NOTE

This Microfiche meets the quality requirements of the American National Standard for Microfiche of Documents (ANSI PH5.9-1975). However, because of imperfections in the document from which it was made, it contains images that are illegible or difficult to read. The source document for this microfiche is the best copy that could be obtained prior to filming.

Congressional Information Service, Inc
Washington, D.C

CIS

TAXPAYER PRIVACY ISSUES

HEARING
BEFORE THE
SUBCOMMITTEE ON OVERSIGHT
OF THE
COMMITTEE ON WAYS AND MEANS
HOUSE OF REPRESENTATIVES
NINETY-SEVENTH CONGRESS
FIRST SESSION

DECEMBER 14, 1981

Serial 97-36

Printed for the use of the Committee on Ways and Means

U.S. GOVERNMENT PRINTING OFFICE
90-425 O WASHINGTON : 1982

H781-13

COMMITTEE ON WAYS AND MEANS

DAN ROSTENKOWSKI, Illinois, *Chairman*

SAM M. GIBBONS, Florida
J. J. PICKLE, Texas
CHARLES B. RANGEL, New York
FORTNEY H. (PETE) STARK, California
JAMES R. JONES, Oklahoma
ANDY JACOBS, JR., Indiana
HAROLD FORD, Tennessee
KEN HOLLAND, South Carolina
WILLIAM M. BRODHEAD, Michigan
ED JENKINS, Georgia
RICHARD A. GEPHARDT, Missouri
THOMAS J. DOWNEY, New York
CECIL (CEC) HEFTEL, Hawaii
WYCHE FOWLER, JR., Georgia
FRANK J. GUARINI, New Jersey
JAMES M. SHANNON, Massachusetts
MARTY RUSSO, Illinois
DON J. PEASE, Ohio
KENT HANCE, Texas
ROBERT T. MATSUI, California
DON BAILEY, Pennsylvania
BERYL ANTHONY, JR., Arkansas

BARBER B. CONABLE, JR., New York
JOHN J. DUNCAN, Tennessee
BILL ARCHER, Texas
GUY VANDER JAGT, Michigan
PHILIP M. CRANE, Illinois
BILL FRENZEL, Minnesota
JAMES G. MARTIN, North Carolina
L. A. (SKIP) BAFALIS, Florida
RICHARD T. SCHULZE, Pennsylvania
BILL GRADISON, Ohio
JOHN H. ROUSSELOT, California
W. HENSON MOORE, Louisiana

JOHN J. SALMON, *Chief Counsel*
JOSEPH K. DOWLEY, *Assistant Chief Counsel*
ROBERT J. LEONARD, *Chief Tax Counsel*
A. L. SINGLETON, *Minority Chief of Staff*

SUBCOMMITTEE ON OVERSIGHT

CHARLES B. RANGEL, New York, *Chairman*

SAM M. GIBBONS, Florida
J. J. PICKLE, Texas
ED JENKINS, Geogia
FRANK J. GUARINI, New Jersey
JAMES M. SHANNON, Massachusetts
MARTY RUSSO, Illinois

PHILIP M. CRANE, Illinois
W. HENSON MOORE, Louisiana
JOHN J. DUNCAN, Tennessee
JAMES G. MARTIN, North Carolina

CONTENTS

Page

Press release of Thursday, December 3, 1981, announcing hearing 1

WITNESSES

U.S. General Accounting Office, General Government Division: William J. Anderson, Director, John Gunner, Evaluator in Charge, and Kenneth Mead, Senior Attorney 87

Internal Revenue Service: Roscoe L. Egger, Commissioner of Internal Revenue, Thomas J. Clancy, Director, Criminal Investigation Division, and Peter V. Filpi, Director, Disclosure Litigation Division 131

Department of Justice: Edward Schmults, Deputy Attorney General 158

Alexander, Donald C., Washington, D.C 56

American Bar Association, John S. Nolan and John B. Jones, Jr 174

American Civil Liberties Union, John H. F. Shattuck and Wade J. Henderson. 73

Burch, Michael S., National Taxpayers Legal Fund 188

Chamber of Commerce of the United States, Edwin S. Cohen and David E. Franasiak 183

Clarke, Owen L., Department of Revenue, Commonwealth of Massachusetts 147

Cohen, Edwin S., Chamber of Commerce of the United States 183

Cohen, Sheldon, Washington, D.C 53

Franasiak, David E., Chamber of Commerce of the United States 183

Gustafson, Charles H., Washington, D.C 68

Hansen, Hon. George, a Representative in Congress from the State of Idaho 46

Henderson, Wade J., American Civil Liberties Union 73

Jones, John B. Jr., American Bar Association 174

Kurtz, Jerome, Washington, D.C 60

Massachusetts, Commonwealth of, Department of Revenue, Owen L. Clarke 147

National Taxpayers Legal Fund, Michael S. Burch 188

Nolan, John S., American Bar Association 174

Nunn, Hon. Sam, a U.S. Senator from the State of Georgia, ranking minority member, Permanent Subcommittee on Investigations, Committee on Governmental Affairs 3

Shattuck, John H. F., American Civil Liberties Union 73

Steinberg, Marty, Permanent Subcommittee on Investigations, Committee on Governmental Affairs, U.S. Senate 3

SUBMISSIONS FOR THE RECORD

Federal Law Enforcement Officers' Association, David S. Heller on behalf of Jack B. Solerwitz, letter 192

Maine, State of, Department of Finance and Administration, Rodney L. Scribner, letter 192

Maryland, State of, Stephen H. Sachs, attorney general, letter 193

National Association, of Tax Administrators, Leon Rothenberg, letter and statement 154

Nevada, State of, Governor Robert List, letter 194

Roth, Hon. William V., Jr., a U.S. Senator from the State of Delaware, statement 190

Rudman, Hon. Warren B., a U.S. Senator from the State of New Hampshire, statement 191

APPENDIX

Page
Comparison of proposals relating to the disclosure of tax information for purposes of nontax criminal law enforcement 195
Tax return confidentiality: A summary of the existing law and its recent consideration 204

TAXPAYER PRIVACY ISSUES

MONDAY, DECEMBER 14, 1981

House of Representatives,
Committee on Ways and Means,
Subcommittee on Oversight,
Washington, D.C.

The subcommittee met at 10:25 a.m., pursuant to notice, in room 2167, Rayburn House Office Building, Hon. Charles B. Rangel (chairman of the subcommittee) presiding.

[Press release announcing hearing and background information follows:]

[Press release of Thursday, Dec. 3, 1981]

HON. CHARLES B. RANGEL, DEMOCRAT OF NEW YORK, CHAIRMAN, SUBCOMMITTEE ON OVERSIGHT, COMMITTEE ON WAYS AND MEANS, U.S. HOUSE OF REPRESENTATIVES, ANNOUNCES HEARINGS ON TAXPAYER PRIVACY ISSUES

Ways and Means Oversight Subcommittee Chairman Charles B. Rangel (D-N.Y.) announced today that the subcommittee will hold a hearing Monday, December 14, 1981, to examine certain taxpayer privacy issues. The Subcommittee will review the existing tax code provisions under Section 6103(i) which allow the Internal Revenue Service to disclose, in certain circumstances, tax returns and return information to federal law enforcement agencies for use in connection with the investigation and prosecution of non-tax crimes. The hearing will begin at 10:00 a.m. on December 14, 1981, in Room 2167 of the Rayburn House Office Building.

Prior to the Tax Reform Act of 1976, tax records could be disclosed in accordance with regulations approved by the President. In response to reports that tax information was being abused and a widespread concern that taxpayers' rights to privacy were not being protected, Congress enacted legislation to safeguard the confidentiality of tax returns by limiting the IRS's authority to disclose such information. Since the statutory provisions of the Internal Revenue Code, Section 6103(i), have been in place now for almost five years, these rules merit comprehensive Congressional review.

The Subcommittee intends to examine:

(a) The extent to which I.R.C Section 6103(i) has served to protect taxpayers from unwarranted governmental intrusion resulting from their compliance with the tax laws.

(b) Whether I.R.C. Section 6103(i) has provided an appropriate balance between taxpayers' rights to privacy and the law enforcement agencies' investigative needs.

(c) The Administration's efforts to coordinate and to operate fully and efficiently within the parameters of the law.

(d) How various proposed changes to existing law would affect current disclosure practices, taxpayer compliance, and law enforcement efforts.

Witnesses will include representatives from the Departments of Treasury and Justice, the General Accounting Office and other interested parties.

Details for submission of requests to be heard

Individuals and organizations interested in presenting oral testimony at this hearing should submit their requests to be heard by telephone (202) 225-3625. A follow-up letter should be sent to John J. Salmon, Chief Counsel, Committee on Ways and Means, U.S. House of Representatives, 1102 Longworth House Office Building, Washington, D.C. 20515. Requests to be heard must be received no later than the close of business Wednesday, December 9, 1981. Requests received after that time may not be honored. Notification to those scheduled to appear will be made as promptly as possible after December 9, 1981.

Due to the limited time available to the Subcommittee for these hearings and the anticipated volume of requests to be heard, we require that all persons and organizations having a common position make every effort to designate one spokesperson to represent them in order for the Subcommittee to hear as many points of view as possible. Every effort will be made to schedule those requesting to testify. However, those not scheduled to present oral testimony may submit written testimony as described below. Time for oral presentations will be strictly limited to the issues as defined above with the understanding that a more detailed statement can be submitted for the hearing record. This will afford time for interrogation of witnesses by Members of the Subcommittee.

Procedures to be followed for submitting testimony

The following is an outline of the procedure to be followed by organizations and individuals who may either want to appear and testify or file a written statement for the record of the proceedings. All requests to be heard should also contain the following information:

1. The name of the witness, title, address, firm, affiliation and/or organization being represented (as well as a telephone number at which the witness or designated representative may be reached).
2. If appearing in an individual capacity, a list of any clients at whose request or in whose employ the witness appears.
3. A topical outline or summary of comments and recommendations.

The above information should also be incorporated in the prepared statements to be presented in person as well as those filed for the printed record.

In order to assure the most productive use of the limited amount of time available to question hearing witnesses, witnesses scheduled to appear before the Subcommittee are required to submit 50 copies of their prepared statement to the full Committee office, Room 1102 Longworth House Building, at least 24 hours in advance of their scheduled appearance. Failure to comply with this requirement may result in the witness being denied the opportunity to testify in person.

Written statements in lieu of personal appearance or submission of additional materials for the record.

For those who wish to file a written statement or supply additional materials for inclusion in the printed record of the hearings, five copies are required and may be submitted at any time prior to the close of business February 1, 1982.

Chairman **Rangel**. The Subcommittee on Oversight will now come to order.

We are here today to examine the operation of a very important Tax Code provision—Internal Revenue Code section 6103(i), which deals with the release of tax information by the IRS for use in connection with Federal law enforcement agency investigations and prosecutions of nontax crimes. This section of the tax law explicitly limits the IRS's authority to disclose tax returns and related information to Federal law enforcement agencies and sets forth certain prerequisite steps that must be taken by such a law enforcement agency before obtaining the information.

The extent to which the IRS should be able to disclose tax information has long been a subject of controversy. In 1976, Congress acted to proscribe tax disclosure except in a limited number of situations. The purpose of this legislation, clearly, was to protect taxpayers from unwarranted release of the confidential statements and materials which taxpayers are required, by law, to supply the IRS each year. In recognizing that there may be compelling criminal cases for which it would be proper for the IRS to share tax information with Federal law enforcement agencies, Congress provided several carefully drafted procedures by which tax returns and tax information may be released. As a result, current law gives the IRS authority to release tax returns or taxpayer-supplied information to a law enforcement agency upon court order. Upon written request, other tax information can be disclosed. Importantly, all will agree that section 6103 is a delicately balanced piece of legislation designated to safeguard taxpayers' rights to privacy against unwarranted governmental intrusion.

The Conference Report for the Economic Recovery Tax Act of 1981 instructed the tax-writing committees to hold timely hearings to thoroughly examine the disclosure rules and the appropriateness of further legislative action. In light of this directive and the subcommittee's longstanding concern with the range of issues surrounding section 6103, these hearings are particularly appropriate. Proposals to change 6103(i) are currently before the Congress. Consequently, the subcommittee has a clear responsibility to take a good, hard look first, at how the current statute is, and has been, working, and then, at the presumptions and underlying issues upon which such proposals for legislative change are based. Only after a definitive case is made for changing current law, are legislative alterations proper.

This is the purpose of these hearings—to examine, from square one:

First, the extent to which Internal Revenue Code section 6103(i) has served to protect taxpayers from unwarranted governmental intrusion resulting from their compliance with the tax laws.

Second, whether Internal Revenue Code section 6103(i) has provided an appropriate balance between taxpayers' rights to privacy and the law enforcement agencies' investigative needs.

Third, the administration's efforts to coordinate and to operate fully and efficiently within the parameters of the law.

Fourth, how various proposed changes to existing law would affect current disclosure practices, taxpayer compliance, and law enforcement efforts.

On behalf of this subcommittee, I would like to extend to our witnesses our welcome and appreciation for the assistance you are providing us here today on a matter which is so crucial to individual rights and law enforcement needs.

I look forward to hearing from each of you.

Congressman Pickle.

Mr. PICKLE. Mr. Chairman, I have no statement at this time.

Chairman RANGEL. Mr. Crane.

Mr. CRANE. I, too, Mr. Chairman, have no questions at this time, and I am prepared to proceed.

Chairman RANGEL. Senator Nunn, thank you for your patience and indulgence in starting late. I know your interest and your success in the Senate in telling your colleagues that meaningful changes have to be made. You were privy to the discussions that took place in the Congress as related to the tax bill. We are anxious that the House meet you halfway in order to determine our responsibilities to change the laws if needed. We do hope that our staffs will be working closely with your staffs so we can see what legislation is needed and how we can work with you on that.

STATEMENT OF HON. SAM NUNN, A U.S. SENATOR FROM THE STATE OF GEORGIA, ACCOMPANIED BY MARTY STEINBERG

Senator NUNN. Thank you very much, Congressman Rangel, Congressman Pickle, Congressman Crane, Congressman Shannon, and Congressman Jenkins. I am delighted to have a chance to be here today. Starting 25 minutes after the hour is about 15 or 20 minutes ahead of the usual Senate hearing, so I feel like you are early rather than delayed here.

I am delighted to have a chance to appear at the beginning of the subcommittee's discussion on this very important piece of legislation and on the provisions of 6103(i) of the Tax Reform Act of 1976. I have a lengthy statement, and I would like to enclose the whole thing in the record, but I will be reading excerpts from the statement. I will be following down the statement in the same sequence it is written, but if it will help the subcommittee follow it, I will be glad to make reference to the page so you can follow it.

Chairman RANGEL. That would help. Without objection, your full statement will appear in the record.

Senator NUNN. Thank you, Mr. Chairman. As you know, I have introduced in the Senate S. 732, which is a bill to modify those disclosure provisions of the 1976 act as they relate to nontax criminal information. A bill identical to S. 732 was introduced in the House as H.R. 1502 by Congressman Gibbons on January 29, 1981. Both of these bills attempt to remedy serious problems concerning the role of the Internal Revenue Service in Federal law enforcement efforts. Both bills attempt to make these changes while retaining the essence of what the Tax Reform Act of 1976 tried to accomplish in terms of privacy and tax returns.

The amendment is an outgrowth of extensive work done by the Permanent Subcommittee on Investigations, of which I was honored to serve as chairman during the 96th Congress.

The rest of page 2 and the top of page 3 give you a detailed analysis of those hearings. We have had 8 or 10 detailed hearings that touched on the this subject matter. Those pages will reference that and I will go to page 3.

Prosecutors and others involved in Federal law enforcement testified before our subcommittee that they were hindered in doing financial investigations by the reluctance of IRS to lend them a hand in attacking those who call the shots in organized crime and narcotics trafficking. This testimony was given to the Subcommittee on Investigations not only in the illegal narcotics profits hearing in 1979, but in virtually every hearing we have conducted over the past 3 years concerning law enforcement issues. Again and again, when we held hearings on organized crime and the use of violence in 1980—I know Congressman Pickle has done a tremendous amount of work in that area—when we held hearings on the Labor Department's investigation of the Central States Pension Fund in 1980, in hearings on waterfront corruption in 1981 and, most recently, again in hearings on international narcotics trafficking last November, we have heard the same refrain: The withdrawal of IRS from joint law enforcement investigations of organized crime, labor racketeers, and narcotics traffickers has had a severely adverse effect upon law enforcement efforts against these criminal groups.

We found that there were two prime reasons for this withdrawal by the IRS. One was the disclosure provisions of the Tax Reform Act of 1976. The other was a general attitude on the part of IRS officials that the agency should only collect taxes and not serve in any capacity as a nontax law enforcement agency. I know you will be hearing testimony, sincere testimony strongly held on that point from other witnesses.

The disclosure provisions of the Tax Reform Act of 1976 are found in section 6103 of the Internal Revenue Code of 1954 (26 U.S.C. 6103). They were enacted in the dying days of the 94th Congress and were intended to avoid future abuses of a "Watergate" nature.

I think just briefly we ought to look back at what the origin of the main source of that abuse was alleged to be. During the Watergate investigations it was revealed that the Nixon White House had used tax returns to pressure potential campaign contributors and certain other individuals who were on a White House "enemies list," and that the administration had ordered IRS to conduct audits of its "enemies." I condemned that at the time on both sides of the aisle and I would want to retain any provision in the law that would diminish the prospects of that happening again. But I want to point out, Mr. Chairman, that the Permanent Subcommittee on Investigations has been unable to document any abuse of tax information on the part of a Federal prosecutor.

The "Watergate abuses" were political abuses, not law enforcement abuses. A study done for Congress in 1976 by the Congressional Research Service and entitled, "Internal Revenue Service: History and Matters Dealing with Oversite of its Practices and Procedures," shows that not only was the attempted misuse of IRS information political in nature, but also that the White House failed miserably in its attempt to misuse the IRS.

Yet although the problem in 1976 was political, we did not even address the problem of political abuse in the Tax Reform Act of 1976. At least it did not do so in a thorough and comprehensive way. The Commissioner of the Internal Revenue Service frankly admitted in his testimony before the Permanent Subcommittee on Investigations that the Watergate abuses which spawned the Tax Reform Act were not even addressed by the act. He said that today, as the law now stands, and this is a continuing situation as we sit here this morning, if the President told him to go out and audit political enemies, there is nothing whatsoever in the Tax Reform Act that prohibits this. If there is any violation of law there it is under other provisions of the law which relate to abuse of criminal process, but not under the Tax Reform Act of 1976.

But to cure these perceived abuses, the Tax Reform Act made tax returns and most other information gathered by the IRS confidential and subject to disclosure by IRS only in accordance with very strict procedures. These procedures apply across the board and govern disclosure to all Federal agencies. They are so sweeping that they can be compared to the use of a sledge hammer to kill an ant.

IRS agents are forbidden to disclose, on their own initiative, any tax return or tax return information, which is any information they gather in connection with a tax return, or taxpayer return information, which is any information they obtain from a taxpayer or his representative, such as his attorney or accountant.

Let us say, for example, that IRS agents conduct an audit of the bank records of a taxpayer, and they discover in his checking account statements that he has made a series of unexplained cash deposits. This may very well lead them to suspect that he has been dealing in narcotics. If they tell the Drug Enforcement Administration about this evidence, however, they would be guilty of a felony under the Tax Reform Act.

Because of the nontax criminal disclosure provisions in section 6103(i), the average citizen is now the main target for IRS's resources. The testimony and statistics developed by the 1980 hearings bear this out. Since the 1976 act, IRS efforts in organized crime cases had dropped over 50 percent. Since the 1976 act, IRS efforts against major narcotics traffickers had dropped almost 75 percent. In the fiscal year 1979, IRS could only confirm 9 or 10 convictions against major narcotics dealers. This is despite the fact that narcotics generate $44 to $63 billion a year, in large measure not taxed.

I have a good many examples of the specific abuses that have taken place under this act, and I think it would be instructive for the committee to examine those at some point. I will not go into detail on those. There is one example after another. We have had much testimony as to specific examples of where the Tax Reform Act basically precludes meaningful cooperation and prosecution. I will go over that information very rapidly and pass on to page 9.

It is possible, of course, for other agencies to obtain tax returns and other IRS-gathered information under section 6103. However, they must apply for a court order in order to get tax returns, and they must make written requests to obtain other IRS information about nontax crimes such as forgery, bribery, or narcotics violations that comes from sources other than tax returns.

In either situation, the requesting agency must describe the information it seeks to obtain.

The court order and written request requirements have created a catch 22 situation. Since IRS agents are forbidden to tell the other agencies of the criminal evidence they gather, it is virtually impossible for these other agencies even to know that such information exists, much less to describe that information with such particularity that they can satisfy the requirements for a court order or written request.

In other words, section 6103 required Federal investigative agencies to go through elaborate request procedures to obtain information that they may not even know that IRS has.

Section 6103 is only a part of the reason why IRS dropped out of the cooperative law enforcement community. Another part of the problem is the attitude of the top officials of the IRS and the policies and procedures they adopted in interpreting and applying section 6103.

Between 1974 and 1980, a series of IRS Commissioners and their top aides took the view that IRS should stick to tax administration—by which they meant tax collection and only tax collection—and out of the general law enforcement arena.

The IRS decision to stick with tax collection only and to avoid criminal law enforcement was welcomed by some who believe that the only proper function of the IRS is tax administration. But these people ignore the simple fact that tax administration goes hand in hand with criminal enforcement. The IRS has been and always will be involved in criminal law enforcement because tax evasion is the end result of any crime that is committed for profit. The question is not whether we want IRS to be involved in law enforcement, for they always have been and always will be. The question is, whom do we want IRS to concentrate its criminal enforcement efforts on? I submit that Congress has, in enacting the disclosure provisions of the Tax Reform Act in 1976, caused IRS to aim its many powerful resources at the average taxpayer who earns his money in a law-abiding manner.

I think it is important to take a look at the IRS internal breakdown between what we call the GEP and the SEP. The IRS's criminal enforcement is split into two divisions. One is called the general enforcement program (or GEP); the other is called the special enforcement program (or SEP).

The GEP concentrates its efforts on the average taxpayer and businessman who earn their money in a law-abiding manner. IRS has always handled this law enforcement responsibility in house, so to speak. That is, to investigate a person or business which earns his or its money legally but may still have a tax problem, IRS does not need the assistance, cooperation, or exchange of information with the FBI, the DEA, or the Criminal Division of the Department of Justice.

On the other hand, the special enforcement program division concentrates its efforts on drug dealers, organized crime figures, pornographers, and other criminals who earn their money from illegal criminal ventures. To pursue this type of individual, IRS needs the assistance of and an exchange of information with the agencies that investigate and prosecute these criminals—agencies such as the FBI, the DEA, and the Criminal Division of the Justice Department.

We want the resources of the IRS focused on the criminals who pay no taxes on their tremendous ill-gotten gains, not on the ordinary taxpayer. Obviously, IRS must be aggressive in collecting the Nation's taxes, but we understand the skepticism of a small-town waitress who is caught for underreporting her tips when organized crime millionaires escape without reporting a cent of their illegal income.

Paying attention only to ordinary taxpayers is not a better way of keeping the voluntary tax collection system working than cracking down on organized criminals who pay no taxes on their criminal profits. The normal taxpayer neither knows nor cares what the Tax Reform Act says. He is motivated by two things: civic duty and fear. The normal taxpayers—and I might add that IRS Commissioners themselves have testified to this—are motivated by their civic duty to support their Government through their tax dollars and by their fear of getting caught if they cheat.

It is my opinion, shared by many others, that the disclosure provisions of the Tax Reform Act not only do not reinforce these motivating factors, but they virtually eliminate them.

I know of no better method to encourage voluntary compliance than to have the front pages of our newspapers filled with a story of how IRS investigated and prosecuted a high-ranking member of organized crime.

Our subcommittee concluded that if the average taxpayer knows that IRS can successfully collect taxes from the mob, he is a lot more likely to ante up his fair share.

When he sees a drugpusher prosecuted as the result of work by the IRS, he is likely to have confidence in our voluntary tax collection system and feel that his taxes are being well spent, especially on law enforcement. On the other hand, if he sees criminals getting away with tax evasion on top of murder and extortion, his natural skepticism toward our tax policy will increase.

Let me try to dispel some of the unfounded fears of our disclosure amendment by explaining how its provisions will protect the privacy of tax returns and other information supplied to IRS. I believe that once these provisions are understood—and I admit this is an intricate, sometimes confusing area of the law—they will be accurately seen for their privacy merits as well as their attempt to improve law enforcement.

First, I want to point out that these amendments to the 1976 Act leave intact the vast majority of that act as it now exists. They do not alter the provisions of the 1976 Act which prohibit loose distribution to government agencies. The amendments are aimed at one isolated, specific subsection of the Tax Reform Act disclosure provisions which, in effect, prohibits the IRS from cooperating and exchanging information with other Federal law enforcement agencies.

Second, and I think this is very important, the amendments give IRS no additional power or authority whatsoever. The amendments do not alter the ability or power of IRS to transfer information concerning the average citizen who earns his money legally and is handled in the IRS's GEP Division, as I have explained already. The amendments merely allow the IRS to cooperate and exchange information under a very carefully restricted legislative scheme involving court orders and formal written requests concerning criminals who earn their money from illegal means.

Third, some people think that individuals have a fifth amendment privilege against self-incrimination with respect to the filing of a tax return. The U.S. Supreme Court, however, contradicts this view. While taxpayers in general do have a fifth amendment privilege against self-incrimination, this privilege does not protect any taxpayer from his obligation to file a return or from his obligation of including all of his correct income figures on the return. In other words, Mr. Chairman, this act as we intend to amend it if we can get it passed does not change the Internal Revenue Service powers in gathering information. It does have an effect on what they can do with that information in the case of nontax crimes. It also would not change the IRS mechanisms for dealing with tax crimes, including tax evasion. I stress that what we are talking about is nontax crime information which they may now have.

Let us look at the judicial standards that the Justice Department would have to meet before it could gain access to the information protected by court order. In order to obtain an ex parte order, Justice Department attorneys would have to present information believed to be reliable that establishes reasonable cause to believe that a specific criminal act has been committed. Those attorneys would have to certify that the information is sought exclusively for use in a Federal criminal investigation or proceeding, and they would have to establish to the satisfaction of a district judge or magistrate that there is reasonable cause to believe that the information may be relevant to a matter relating to the commission of the criminal act.

These are essentially the same standards that must be met under Federal law in order for authorities to wiretap our telephones or put listening devices in our homes and offices. It seems to me that if these standards are sufficient to protect the privacy of our most personal conversations, they also are sufficient to protect our tax information.

In addition to these privacy protections, I would point out that our bill—unlike the existing provision of the law—would channel all requests for IRS information through the Justice Department. Only one agency under our approach would be permitted to obtain tax information, and the requesting official in every case would be a Government attorney.

In other words, Mr. Chairman, our disclosure amendment is laden with safeguards for the privacy of all information we can reasonably expect to keep private. There will be no wholesale scrapping of privacy here. There will be no "sellout" to a few law enforcement authorities who might like to see their work made easier. There certainly will be no attempt here to create a breeding ground for a repeat of the so-called Watergate abuses.

The only people in my view that need fear this legislation are narcotics traffickers and organized crime figures and white collar criminals who are cheating other taxpayers by not paying their fair share.

This amendment would give no additional power or abilities to IRS to gather information about ordinary taxpayers.

The ordinary citizen is and always will be handled "in house" by the IRS with no need for cooperation with the FBI or DEA. On the other hand, criminal tax evaders, who earn their money by participating in a life of crime, would receive different treatment by IRS. In cases where criminal ventures generate profits, IRS must have the capability to cooperate with and exchange information with the Federal investigative and prosecutive agencies.

It is in this very small area—criminal tax evaders—that we seek our primary change so that IRS and other Federal law enforcement agencies can work even more effectively together against these criminals than they can today.

There are certain civil and criminal damage provisions that we change here that I think are important. The Tax Reform Act of 1976 contains severe criminal and civil penalties for persons who disclose tax returns or related information in violation of the act.

The civil damage provision, 26 U.S.C. 7217, makes any person who willfully or negligently discloses a tax return or tax return information in violation of the act personally liable for civil damages in a suit brought against him by the taxpayer.

Existing law provides that there is no civil liability for disclosures which result from good faith, but wrong, interpretations of the act.

The criminal provision proposes a good-faith defense for a criminal violation which I think is a reasonable approach to this problem.

Mr. Chairman, for generations the Internal Revenue Service led the way in this Nation's battle against organized crime and narcotics trafficking, but since 1977 it has hidden behind the disclosure provisions of the Tax Reform Act to stay out of the fray.

It is now time for us to decide that IRS shall become once again the effective force for justice that it was in the days of bootleggers and rumrunners. Our proposals will send IRS a clear and unmistakable signal that it should do just that.

We have spent many long hours in drafting what we feel is a very well reasoned amendment. We will retain very important privacy safeguards that will prevent any repetition of Watergate-type abuses that were covered by the original law, though I repeat that the most notorious abuse was not covered by the original law. At the same time, we put a duty on IRS to cooperate once again with the fight against the ever-increasing organized crime and narcotics problems facing the Nation.

Five years of inactivity by this once effective law enforcement agency is enough. It is time to act.

Mr. Chairman, my full statement, together with a section-by-section analysis of S. 732, which is identical to H.R. 1502, and a comparison of that bill to existing law appears in the March 17, 1981, Congressional Record. I would like to present a copy of that for the record of these hearings.

I thank you and the subcommittee for this opportunity to discuss the provisions of H.R. 1502, and I would be pleased to answer any questions you may have.

Mr. Chairman, that concludes my testimony. I apologize for the length, but it was very difficult to cover this complex area in a more abbreviated fashion.

[The prepared statement follows:]

STATEMENT OF HON. SAM NUNN, A SENATOR FROM THE STATE OF GEORGIA

Mr. Chairman, I am delighted to appear here today at the opening of this subcommittee's hearings on the disclosure provisions of section 6103(i) of the Tax Reform Act of 1976. As you know, I have introduced in the Senate S. 732, which is a bill to modify those disclosure provisions of the 1976 Act as they relate to non-tax criminal information. A bill identical to S. 732 was introduced in the House as H.R. 1502 by Congressman Gibbons on January 29, 1981. Both of these bills attempt to remedy serious problems concerning the role of the Internal Revenue Service in federal law enforcement efforts.

I should add that S. 732 was passed by the Senate on July 27, 1981, as Amendment No. 492 to the Economic Recovery Tax Act of 1981. A similar amendment was not enacted by the House of Representatives, however. The Conference Report concerning these provisions recommended full hearings on H.R. 1502 in the House and on its companion bill, S. 732, in the Senate prior to passage. I want to thank you, Mr. Chairman, as well as the full Subcommittee and staff, for the prompt scheduling of these hearings.

I would like to take this opportunity to offer my own comments both as to the factual evidence which I believe supports and necessitates the passage of H.R. 1502 and also concerning the provisions of the bill.

This amendment is an outgrowth of extensive work done by the Permanent Subcommittee on Investigations, of which I was honored to serve as Chairman during the 96th Congress.

Our Subcommittee spent 1979, 1980 and 1981 investigating various aspects of organized crime, labor racketeering, and narcotics trafficking. As I look back on our studies and hearings, I am astounded at the size and sophistication of these triple menaces to the well-being of our Nation.

The "underground economy" is estimated at upwards of $124 billion a year, of which the traffic in illegal narcotics amounts to somewhere between $44 billion and $63 billion. Included in these astronomical figures are an estimated $25 billion to $50 billion in unreported and untaxed profits. In other words, we may not have had a deficit last year if taxes has been paid on these illegal profits.

All of this money has had a tremendous inflationary impact on the economy of several regions of the country, especially Florida, Texas and the Southwest areas bordering Mexico. Even my homestate of Georgia has experienced an increase in narcotics trafficing, for as enforcement authorities have cracked down on smuggling into Florida from South America, many traffickers have moved their operations northward.

The Permanent Subcommittee on Investigations explored this problem extensively, and in December of 1979 we conducted very thorough hearings on "Illegal Narcotics Profits." We issued a comprehensive report on this investigation in August 1980. (Senate Report No. 96-887).

It has long been recognized that financial investigations, relying on financial and tax records, are one of the most effective tools in piercing the veil of secrecy that protects those at the top of any organized crime ring—be it a drug smuggling operation or a traditional organized crime family.

Indeed, it was the ability of the Internal Revenue Service to conduct sophisticated financial investigations that sent such notorious mobsters as Al Capone and Frank Costello to jail on income tax evasion charges when other agencies were unable to gather enough evidence of non-tax crimes to have them indicted; much less convicted.

We found, however, that even though organized crime and narcotics trafficking have become bigger and more sophisticated than ever before, the one law enforcement agency that the kingpin criminals fear most—the IRS—had withdrawn from the fray.

Prosecutors and others involved in Federal law enforcement testified before our Subcommittee that they were hindered in doing financial investigations by the reluctance of IRS to lend them a hand in attacking those who call the shots in organized crime and narcotics trafficking. This testimony was given to the Subcommittee on Investigations not only in the Illegal Narcotics Profits hearing in 1979, but in virtually every hearing we have conducted over the past three years concerning law enforcement issues. again and again, when we held hearings on Organized Crime and the Use of Violence in 1980, when we held hearings on the Labor Department's investigation of the Central States Pension Fund in 1980, in hearings on Waterfront Corruption in 1981 and, most recently, again in hearings on International Narcotics Trafficking last November, we have heard the same refrain: the withdrawal of IRS from joint law enforcement investigations of organized crime, labor racketeers and narcotics traffickers has had a severely adverse effect upon law enforcement efforts against these criminal groups.

We found that there were two prime reasons for this withdrawal by the IRS. One was the disclosure provisions of the Tax Reform Act of 1976. The other was a general attitude on the part of IRS officials that the agency only should collect taxes and not serve in any capacity as a non-tax law enforcement agency.

THE TAX REFORM ACT OF 1976

The disclosure provisions of the Tax Reform Act of 1976 are found in Section 6103 of the Internal Revenue Code of 1954 (26 U.S.C. 6103). They were enacted in the dying days of the 94th Congress and were intended to avoid future abuses of a "Watergate" nature.

Until the act became effective, tax returns were considered to be public records, and access to them was governed by Presidential Executive order. Many Federal agencies, including the White House, had easy access to tax returns for a wide variety of uses.

During the Watergate investigations, it was revealed that the Nixon White House had used tax returns to pressure potential campaign contributors and certain other individuals who were on a White House "enemies list," and that the Administration had ordered IRS to conduct audits of its "enemies."

It also was revealed by the Senate Judiciary Committee that an IRS special service staff collected and disseminated information about thousands of individuals and groups which the IRS considered to have "extremist views and philosophies."

In short, various congressional committees found that tax returns and tax information were made available to a number of Federal agencies for many questionable purposes. I think all of us would agree that such disclosure represented an abuse of taxpayers privacy.

But I want to point out, Mr. Chairman, that the Permanent Subcommittee on Investigations was unable to document any abuse of tax information on the part of a Federal prosecutor.

The "Watergate abuses" were political abuses, not law enforcement abuses. A study done for Congress in 1976 by the Congressional Research Service and entitled, "Internal Revenue Service: History and Matters Dealing with Oversite of its Practices and Procedures," shows that not only was the attempted misuse of IRS information political in nature, but also that the White House failed miserably in its attempt to misuse the IRS.

Yet although the problem in 1976 was political, we did not even address the problem of political abuse in the Tax Reform Act of 1976. The Commissioner of the Internal Revenue Service frankly admitted in his testimony before the Permanent Subcommittee on Investigations that the Watergate abuses which spawned the Tax Reform Act were not even addressed by the Act. He said that today, as the law now stands, if the President told him to go out and audit political enemies, there is nothing whatsoever in the Tax Reform Act that prohibits this.

But to cure these perceived abuses, the Tax Reform Act made tax returns and most other information gathered by the IRS confidential and subject to disclosure by IRS only in accordance with very strict procedures. These procedures apply across the board and govern disclosure to all Federal agencies. They are so sweeping that they can be compared to the use of a sledge hammer to kill an ant.

IRS agents are forbidden to disclose, on their own initiative, any tax return or "tax return information," which is any information they gather in connection with a tax return, or "taxpayer return information," which is any information they obtain from a taxpayer or his representative, such as his attorney or accountant.

Let us say, for example, that IRS agents conduct an audit of the bank records of a taxpayer, and they discover in his checking account statements that he has made a series of unexplained cash deposits. This may very well lead them to suspect that he has been dealing in narcotics. If they tell the Drug Enforcement Administration about this evidence, however, they would be guilty of a felony under the Tax Reform Act.

As a result, there is very little criminal information exchanged today between IRS and the other Federal law enforcement agencies. IRS turned over an average of just 32 pieces of criminal evidence per year during 1977, 1978, and 1979. DEA officials testified at our hearings that they received no non-tax criminal evidence over that same period.

Because of the non-tax criminal disclosure provisions in section 6103(i), the average citizen is now the main target for IRS's resources. The testimony and statistics developed by 1980 bear this out. Since the 1976 Act, IRS efforts in organized crime cases had dropped over 50 percent. Since the 1976 Act, IRS efforts against major narcotics traffickers had dropped almost 75 percent. In the fiscal year 1979, IRS could only confirm 9 or 10 convictions against major narcotics dealers. This is despite the fact that narcotics generate $44 to $63 billion a year.

What happens to the nontax criminal evidence that IRS agents come across during the course of their tax investigations? Apparently, it is buried somewhere in the IRS files.

For example, IRS agents told our Subcommittee that they found evidence of massive embezzlements when they audited a labor union's records, but they could not report this information to the Justice Department. Thus, Justice had no information upon which to begin a nontax prosecution.

In another example, IRS agents found evidence in a taxpayer's business records that a policeman had been bribed. That evidence was never disclosed, and the policeman was still on the job as of last year.

These examples pale in comparison to an incident known as the case of the trash can in which DEA was investigating a chemist suspected of concocting illegal drugs.

DEA learned that an IRS agent had searched the chemist's trash can and had discovered evidence that the chemist indeed was making illegal drugs. However, IRS would not volunteer this evidence to DEA.

The prosecutor subpoenaed the IRS agent and the trash can documents, but IRS cited the Tax Reform Act and refused to let the agent answer the subpoena. IRS said the trash was gathered in connection with the chemist's tax return: therefore, the prosecutor needed a court order under section 6103 to see the documents.

In my mind, by keeping secret this evidence of criminal activity found in a taxpayer's business books and records, bank account statements, and check stubs, we legislated an exemption for criminals.

Our investigation has convinced me that the disclosure provisions of section 6103, coupled with the way they have been interpreted and enforced by IRS, have had a highly detrimental effect on our Federal law enforcement system.

In the hearings before the Permanent Subcommittee on Investigations on Illegal Narcotics Profits, Oliver B. Revell, then the Deputy Assistant Director of the FBI in the Criminal Investigative Division, told us:

"The [1976] act's disclosure provisions often hamper the FBI's investigation of major ongoing white-collar crime and organized crime cases. When disclosure is sought to assist in the timely issuance of search warrants, or other legitimate law enforcement functions, the delays incurred are excessive to the requirement of investigation. When disclosure is sought, delays of three months are common. Delays of six to nine months have been reported on many occasions.

* * * * * * *

"The act has resulted in unnecessary waste of taxpayers' dollars, budget funds and investigative time in that the IRS is usually unable to advise us of the cases on which it is working, which precludes us from obtaining close cooperation with IRS and leads, in some instances, to the FBI unknowingly conducting duplicative investigations. . . . It also leads to us being unable to obtain records which have been previously obtained by the IRS and pertain to [an FBI] ongoing investigation. So it delays our investigation and sometimes causes it to be closed because we cannot obtain records that have already . . . been obtained by IRS, when we didn't know of their investigation until we engaged in our investigation."

The Federal law enforcement system is complex and sophisticated. We do not have a Federal police state. Instead, we have a series of agencies broken down by criminal jurisdiction that must operate with a high degree of coordination and cooperation. It is not unusual, in fact it is quite common, to combine the skills and information of many agencies to achieve any measure of success in criminal enforcement.

IRS has a fine tradition and history of being one of the most effective law enforcement agencies, especially in cases involving high echelon criminals. Obviously, since the purpose of criminal ventures is to make money, very few substantive crimes can be committed without some tax consequence. Therefore, IRS always has been—and continues to be—a key agency both in terms of financial expertise and in terms of financial information.

The language and interpretation of the Tax Reform Act, however, have caused a severe breakdown in our delicate and complex Federal law enforcement system. It has taken up to 13 months simply to receive the assistance of IRS agents in joint investigations. The Tax Reform Act and its interpretation by IRS has caused a bureaucratic nightmare in cases where Federal agencies should willingly assist each other. Moreover, the Tax Reform Act and its interpretations by IRS have posed terrible dilemmas for IRS agents who must ignore the dictates of justice for every other American, and refuse to turn over evidence of serious crimes to the appropriate authorities.

THE "CATCH 22"

It is possible, of course, for other agencies to obtain tax returns and other IRS-gathered information under section 6103. However, they must apply for a court order in order to get tax returns, and they must make written requests to obtain other IRS information about non-tax crimes such as forgery, bribery, or narcotics violations that comes from sources other than tax returns.

In either situation, the requesting agency must describe the information it seeks to obtain.

The court order and written request requirements have created a "Catch 22" situation. Since IRS agents are forbidden to tell the other agencies of the criminal evidence they gather, it is virtually impossible for these other agencies even to know that such information exists, much less to describe that information with such particularity that they can satisfy the requirements for a court order or written request.

In order words, section 6103 required federal investigative agencies to go through elaborate request procedures to obtain information that they may not even know that IRS has.

Just last month the Permanent Subcommittee on Investigations listened to testimony from Jay Ethington, an Assistant U.S. Attorney for the Northern District of Texas. Mr. Ethington has been a prosecutor for 10 years and has prosecuted about one hundred different narcotics traffickers. When we asked him about this aspect of non-tax disclosure, he stated:

"We have a provision in the disclosure aspect of the Tax Reform Act that says I can gain the authority to get disclosure from IRS agents by going to a Federal judge and getting a court order, but before I can get that court order, I have to get authority from the Department of Justice. To get that authority, I must disclose the information that the IRS agent has that he is going to give me, but he won't give that to me until we get authority. So we are in a Catch-22 situation."

This "Catch-22" situation has made it all but impossible for the FBI, DEA, and other agencies to receive the necessary information and cooperation from the IRS.

IRS ATTITUDE

Section 6103 is only a part of the reason why IRS dropped out of the cooperative law enforcement community. Another part is the attitude of the top officials of the IRS and the policies and procedures they adopted in interpreting and applying section 6103.

Between 1974 and 1980, a series of IRS commissioners and their top aides took the view that IRS should stick to "tax administration"—by which they meant tax collection and only tax collection—and out of the general law enforcement arena.

The IRS decision to stick with tax collection only and avoid criminal law enforcement was welcomed by some who believe that the only proper function of the IRS is tax administration. But these people ignore the simple fact that tax administration goes hand in hand with criminal enforcement. The IRS has been and always will be involved in criminal law enforcement because tax evasion is the end result of any crime that is committed for profit. The question is not whether we want IRS to be involved in law enforcement for they always have been and always will be. The question is, whom do we want IRS to concentrate its criminal enforcement efforts on? I submit that Congress has, in enacting the disclosure provisions of the Tax Reform Act in 1976, caused IRS to aim its many powerful resources at the average taxpayer who earns his money in a law-abiding manner.

The IRS's criminal enforcement is split into two divisions. One is called the General Enforcement Program (or GEP), the other is called the Special Enforcement Program (or SEP).

The GEP concentrates its efforts on the average taxpayer and businessman who all earn their money in a law-abiding manner. IRS has always handled this law enforcement responsibility "in-house", so to speak. That is, to investigate a person or business which earns his or its money legally but may still have a tax problem, IRS does not need the assistance, cooperation, or exchange of information of the FBI, the DEA, or the Criminal Division of the Department of Justice.

On the other hand, the SEP division concentrates its efforts on drug dealers, organized crime figures, pornographers, and other criminals who earn their money from illegal criminal ventures. To pursue this type of individual, IRS needs the assistance of and an exchange of information with the agencies that investigate and prosecute these criminals—agencies such as the FBI, the DEA, and the Criminal Division of the Justice Department.

We want the resources of the SEP Division focused on the criminals who pay no taxes on their tremendous ill-gotten gains, not on the ordinary taxpayer. Obviously, IRS must be aggressive in collecting the Nation's taxes, but we understand the skepticism of a small town waitress who is caught for under-reporting her tips when organized crime millionaires escape without reporting a cent of their illegal income.

Paying attention only to ordinary taxpayers is not a better way of keeping the voluntary tax collection system working than cracking down on organized criminals who pay no taxes on their criminal profits. The normal taxpayer neither knows nor cares what the Tax Reform Act says. He is motivated by two things: civic duty and fear. The normal taxpayer [and I might add that IRS commissioners themselves have testified to this] state that taxpayers are motivated by their civic duty to support their Government through their tax dollars and by their fear of getting caught if they cheat.

It is my opinion, shared by many others, that the disclosure provisions of the Tax Reform Act not only do not reinforce these motivating factors but they virtually eliminate them.

First, a citizen who sees big-time crooks get away with not only committing the crime but also not having to pay taxes on his illegally gained income grows very cynical about his Government—and rightly so. They honestly feel that if big-time crooks don't pay their taxes, why should they? "Why shouldn't I cheat just like the big-time crooks do?" This cynicism has led us inevitably to our tremendous underground economy. Unfortunately for the average citizen who cheats—he'll find out that IRS's resources are aimed almost entirely at him and not the crooks.

Second, ever since the days of Al Capone and Frank Costello, the average taxpayer has felt—and again, rightly so—if IRS can get the big crooks, the organized crime leaders, they can certainly get me. But, I submit as IRS's efforts have diminished in this area due to our present legislation, the average citizen feels this fear less and less, and has little motive or incentive to honestly fill out his tax returns.

I know of no better method to encourage voluntary compliance than to have the front pages of our newspapers filled with a story of how IRS investigated and prosecuted a high-ranking member of organized crime.

Our Subcommittee concluded that if the average taxpayer knows that IRS can successfully collect taxes from the mob, he is a lot more likely to ante up his fair share—if for no other reason than the fear of being caught.

When he sees a drug pusher prosecuted as the result of work by the IRS, he is likely to have confidence in our voluntary tax collection system and feel that his taxes are being well spent, especially on law enforcement. On the other hand, if he sees criminals getting away with tax evasion on top of murder and extortion, his natural skepticism toward our tax policy will increase.

IRS' recent emphasis on ordinary taxpayers has not increased voluntary compliance with the tax laws. In fact, statistics compiled by both the IRS and the General Accounting Office indicate that voluntary compliance with the tax laws actually has decreased since passage of the Tax Reform Act of 1976 and the subsequent withdrawal of IRS from cooperative law enforcement efforts aimed at big-time criminals.

The GAO findings also refute the contention that voluntary compliance is in direct proportion to the degree of confidentiality of tax return information. If that is so, then the total confidentiality of the Tax Reform Act would have resulted in total compliance. Obviously, it has not.

Other statistics indicated the extent of IRS withdrawal: between 1974 and the first nine months of 1978, the number of organized crime cases which originated from IRS-developed tax information dropped from 620 to just 221.

Partially as a result of our Subcommittee's work, the Carter Administration ordered IRS to step up its investigations of suspected narcotics dealers and organized criminals. IRS has devoted more of its resources to these efforts, and it has adjusted some of its policies and interpretations with respect to the disclosure of non-tax criminal evidence obtained by its agents.

These are steps in the right direction; however, we still need to fine-tune the Tax Reform Act of 1976 in order to remove some serious and unnecessary roadblocks to IRS active participation in federal law enforcement.

DISCLOSURE AMENDMENTS

Our amendments will not scrap the privacy safeguards which were written into the Tax Reform Act, but they will strike a balance so that IRS can and will again cooperate with federal prosecutors.

Let me try to dispel some of the unfounded fears of our disclosure amendment by explaining how its provisions will protect the privacy of tax returns and other information supplied to IRS. I am sure that once these provisions are understood—and I admit this is an intricate, sometimes confusing area of the law—they will be accurately seen for their privacy merits as well as their attempt to improve law enforcement.

First, I want to point out that these amendments to the 1976 Act leave the vast majority of that Act intact. They do not alter the provisions of the 1976 Act which prohibit loose distribution to government agencies. The amendments are aimed at one isolated, specific subsection of the Tax Reform Act disclosure provisions which, in effect, prohibits the IRS from cooperating and exchanging information with other federal law enforcement agencies.

Second, the amendments give IRS no additional power or authority whatsoever. The amendments do not alter the ability or power of IRS to obtain information in any manner. They do not alter the ability of the IRS to transfer information concerning the average citizen who earns his money legally and is handled in the IRS's GEP Division, as I've explained already. The amendments merely allow the IRS to cooperate and exchange information under a very carefully restricted legislative scheme involving court orders and formal written requests concerning criminals who earn their money from illegal means.

Third, some people think that individuals have a Fifth Amendment privilege against self-incrimination with respect to the filing of a tax return. The U.S. Supreme Court, however, contradicts this view. While taxpayers in general do have a Fifth Amendment privilege against self-incrimination, this privilege does not protect any taxpayer from his obligation to file a return or from his obligation of including all of his correct income figures on the return. There is a Fifth Amendment privilege with respect to the source of the income if the money was earned illegally, but no privilege concerning filing completely and accurately. The amendments thus have no effect on any Fifth Amendment privilege.

Let's look at the types of information that could be disclosed only by ex parte court order, just as under existing law. This includes individual tax returns and all supporting attachments, such as W-2 forms, lists of donations to charitable and nonprofit organizations, and various other schedules.

It also includes the returns and supporting documentation of small closely held corporations, partnerships, associations, unions or other entities consisting of no more than two owners or members. In other words, the tax and supporting records of these organizations—in which there is a privacy expectation because they usually are closely owned by only two family members or friends—will be protected just as they are today.

On the other hand, information gathered from other sources, such as from larger corporations or from third parties, such as banks, would not have the same degree of protection. The courts have consistently held that corporate information does not enjoy the same constitutional protections as individual information; nor is there the same practical privacy expectation in corporate records, simply because of the number of people in most corporations who have access to that information. We really cannot expect the same degree of privacy for information about us that is maintained by third parties as we do for information that is in our own possession.

The fact of the matter is that other Government agencies, such as the Securities and Exchange Commission and the Department of Labor have access to similar information concerning entities, but those agencies, unlike IRS, have no disclosure prohibitions to interfere with their referring criminal information to the Justice Department, which they do on a regular basis.

Let us look at the judicial standards that the Justice Department would have to meet before it could gain access to the information protected by court order. In order to obtain an ex parte order, Justice Department attorneys would have to present information believed to be reliable that establishes reasonable cause to believe that a specific criminal act has been committed. Those attorneys would have to certify that the information is sought exclusively for use in a Federal criminal investigation or proceeding, and they would have to establish to the satisfaction of a district judge or magistrate that there is reasonable cause to believe that the information may be relevant to a matter relating to the commission of the criminal act.

These are essentially the same standards that must be met under federal law in order for authorities to wiretap our telephones or put listening devices in our homes and offices. It seems to me that if these standards are sufficient to protect the privacy of our most personal conversations, they also are sufficient to protect our tax information.

In addition to these privacy protections, I would point out that our bill—unlike the existing provision of the tax Reform Act—would channel all requests for IRS information through the Justice Department. Only one agency would be permitted to obtain tax information, and the requesting official in every case would be a government attorney.

In other words, Mr. Chairman, our disclosure amendment is laden with safeguards for the privacy of all information we can reasonably expect to keep private. There will be no wholesale scrapping of privacy here. There will be no "sell-out" to a few law enforcement authorities who might like to see their work made easier. There certainly will be no attempt here to create a breeding ground for a repeat of the so-called Watergate abuses. And there certainly will be no "meat-ax" attempt to butcher the Tax Reform Act.

On the other hand, we believe we offer a vey balanced, well-thought-out effort to fine-tune section 6103 of the Internal Revenue Code, which, as the record clearly indicates, needs to be done.

These amendments are the product of two year's hard work on the part of several congressional subcommittees, the Justice Department, and the IRS itself. They have been developed in the broad daylight with the views of all sides considered.

No one who is concerned about the privacy of tax returns or a repetition of the abuses of tax information should fear this amendment. Hard working, law-abiding taxpayers can be rest assured that the information they supply IRS will remain within that agency where it belongs.

The only people that need fear this legislation are narcotics traffickers and organized crime figures and white collar criminals who are cheating other taxpayers by not paying their fair share.

This amendment would give no additional power or abilities to IRS to gather information about ordinary taxpayers.

The ordinary citizen is and always will be handled "in-house" by the IRS with no need for cooperation with the FBI or DEA. On the other hand, criminal tax evaders, who earn their money by participating in a life of crime, receive different treatment by IRS. In cases where criminal ventures generate profits, IRS must have the capability to cooperate with and exchange information with the federal investigative and prosecutive agencies.

It is in this very small area—criminal tax evaders—that we seek our primary change so that IRS and other federal law enforcement agencies can work even more effectively together against these criminals than they can today. As it now stands, the Tax Reform Act of 1976 makes it much easier for IRS to go after the average taxpayer than the criminal. This is a complete reversal of the societal priorities that we should be encouraging.

CIVIL DAMAGE PROVISIONS

The Tax Reform Act of 1976 contains severe criminal and civil penalties for persons who disclose tax returns or related information in violation of the Act.

The civil damage provision, 26 U.S.C. 7217, makes any person who willfully or negligently discloses a tax return or tax return information in violation of the Act personally liable for civil damages in a suit brought against him by the taxpayer.

Existing law provides that there is no civil liability for disclosures which result from good faith, but wrong, interpretations of the Act.

Our proposed change to section 7217 provides that the Government will be liable for damages awarded against a Federal official or employee so long as the disclosure occurred within the scope of his employment and was not done corruptly, maliciously, in return for anything of value, or willfully in violation of the disclosure provisions of the Act.

We do not believe that IRS agents should be personally liable for damages arising out of disclosures which are not done with wrongful intent, and our proposal spells this out.

CRIMINAL PENALTIES

The criminal penalties of the Tax Reform Act, 26 U.S.C. 7213, make it a felony to willfully disclose tax returns or tax return information in violation of the Act. Persons found guilty can be fined up to $5,000 or sentenced to jail for up to 5 years, or both, and assessed the costs of prosecution.

Under existing law, there is no defense available for good faith but wrong interpretations of the disclosure provisions. As a result, IRS agents testified before our Subcommittee, they will always stay on the safe side of the law and not disclose any IRS information to other agencies except in the most serious situations. The disclosure provisions are not always easy to interpret in every situation when an IRS agent comes across evidence of a nontax crime. In fact, even though IRS has issued a number of "clarifying" interpretations and instructions, its agents testified that they never could be sure if they were violating the Act when they disclosed information. In fact, IRS's own legal counsel had difficulty interpreting the provisions when asked questions at our hearings.

In order to ease the minds of IRS agents and to encourage them to report nonreturn information of possible crimes, we propose that an affirmative defense provision be added to the criminal penalty section to relieve them of criminal liability when they can establish that they made the disclosure based on good faith, though erroneous, interpretation of the disclosure provisions.

CONCLUSION

Mr. Chairman, for generations the Internal Revenue Service led the way in this Nation's battle aginst organized crime and narcotics trafficking, but since 1977 it has hidden behind the disclosure provisions of the Tax Reform Act to stay out of the fray.

It is now time for us to decide that IRS shall become once again the effective force for justice that it was in the days of bootleggers and rumrunners. Our proposals will send IRS a clear and unmistakable signal that it should do just that.

We have spent many long hours in drafting what we feel is a very well-reasoned amendment. We will retain very important privacy safeguards that will prevent any repetition of Watergate-type abuses. At the same time, we put a duty on IRS to cooperate once again with the fight against the every increasing organized crime and narcotics problems facing the Nation.

Five years of inactivity by this once effective law enforcement agency is enough. It is time to act.

Mr. Chairman, my full statement, together with a section-by-section analysis of S. 732, which is identical to H.R. 1502, and a comparison of that bill to existing law appears in the March 17, 1981 Congressional Record. I would like to present a copy of that for the record of these hearings.

I thank you and the Subcommittee for this opportunity to discuss the provisions of H.R. 1502, and I would be pleased to answer any questions you may have.

SECTION-BY-SECTION SUMMARY OF PROPOSED AMENDMENTS TO 26 U.S.C. 6103, 26 U.S.C. 7213, AND 26 U.S.C. 7217

This bill would streamline and clarify provisions of the Internal Revenue Code governing access to tax information for use in non-tax criminal investigations and prosecutions. The bill combines the salient features of Senate-initiated proposals and those developed by the Carter administration. This compromise measure is based on more than eight months of study and hearings by four Congressional committees. Generally, the bill would clarify ambiguities in existing law, refine needlessly cumbersome procedures, and distinguish between privacy rights of individuals as contrasted with those of legal entities such as corporations. The modest changes proposed would substantially assist federal law enforcement authorities in combatting narcotics trafficking, organized crime and white-collar offenses involving large sums of money. At the same time, the bill preserves the safeguards for taxpayer privacy established in 1976.

Definitions of protected information (26 U.S.C. 6103(b)(1-3))

Existing law uses a baffling series of four terms to describe information held by IRS, i.e., "returns," "return information," "taxpayer return information," and "return information other than taxpayer return information." S. 2402 would clarify the law by adopting a workable two-part definitional structure.

Section 1. The new § 6103(b)(1) would describe the first category of protected tax information, "return information," which includes (A) returns of all taxpayers and (B) underlying records and information submitted by or on behalf of "individual taxpayers," to support the filing of a tax return.

Section 2. The second category of information held by IRS, "non-return information," is defined to encompass all information held by IRS not covered by the definition of "return information."

Section 3. The bill defines the term "individual taxpayer" as an individual or a legal entity with no more than two owners, shareholders, or members, such as a small, family-owned business.

Taken together, these three definitions simplify existing law by reducing the number of categories of information from four to two; moreover, the two new categories of information conform to the methods of obtaining access: "return information" requires a court order while "non-return information" may be obtained pursuant to a formal law enforcement request under (i)(2) or pursuant to a report of crime under (i)(3). The only substantive change made by the revised definitional structure is that the books and records of legal entities, such as banks and corporations, are made available under (i)(2) or (i)(3); they are now available only under (i)(1), as are books and records of individuals.

The rationale for the distinction is that natural persons have greater privacy rights than do corporations or other entities. A similar distinction is made in the Privacy Act of 1974 (5 U.S.C. 552a) and the Financial Privacy Act of 1978 (12 U.S.C. 3401-3422), neither of which applies to corporate records. Moreover, records of corporations and other entities are normally subject to inspection by shareholders and others with an interest in the entity, as well as federal, state and local authorities; individual books and records are not. Furthermore, books and records of legal entities are normally maintained for purposes other than tax requirements; individual books and records are frequently maintained solely to comply with tax laws. Finally, the Fifth Amendment privilege against self-incrimination does not extend to legal entities.

For these reasons, S. 2402 accords a higher degree of protection to underlying books and records of individuals than to those of legal entities. Because legal entities comprised of only two persons, such as small, closely-held businesses, are usually the alter ego of an individual, they are treated as individuals. Again, it should be noted that all tax returns are accorded the higher degree of protection without regard to the nature of the taxpayer; the distinction between individuals and entities applies only to underlying information, primarily financial books and records.

Disclosure pursuant to court order (26 U.S.C. 6103(i)(1))

Section 4, Part 1. The revised § 6103(i)(1) preserves the structure of the existing court order provision. The modifications are intended only to clarify existing law and to make the literal terms of the statute comply with actual practice.

For example, the standards in existing (i)(1), if read literally, require a factual showing that cannot be made unless the prosecutor seeking access is already in possession of the information sought. Courts have interpreted this language in a commonsense fashion to require proof only of those facts a federal prosecutor can realistically be expected to demonstrate: that there is reasonable cause to believe a specific federal crime has occurred or is occurring, that there is reasonable cause to believe tax information is relevant to that offense, and that the information will be used exclusively for investigation and prosecution of that offense. S. 2402 would substitute these standards for those of existing law. Because this merely codifies present practice, it has no practical effect on taxpayer privacy or tax administration. It does, however, reduce the potential for widely varying judicial results and the extreme chilling effect that the unrealistic language of current law has on federal prosecutors who need tax information for legitimate law enforcement purposes.

The proposed standard is more reasonable, with the added safeguard of prosecutorial intervention. The main criticism of the present standard was that it was impossible to meet. Therefore, no one used it. Also, the proposed would eliminate the third requirement that the Government prove the financial information cannot be obtained from any other source. The fact is that the financial information is "available" elsewhere, but the Government would have to completely reconstruct a taxpayer's bank records to duplicate the information on the return. This third requirement of the present act also requires the Government to prove that the tax return was the most probative evidence of the crime to be proven. Since this section deals only with non-tax crimes, the tax return itself would never be the most probative evidence of the crime. Only the actual financial records would qualify. Thus an impossible standard would be deleted.

The new (i)(1) modifies the class of federal officials who may authorize an application for a court order. Existing law requires all such applications to be routed through Washington for approval before being presented to the court, a requirement which results in substantial delay and paperwork. The new (i)(1)(B) would permit United States Attorneys and Attorneys-in-Charge of Organized Crime Strike Forces in the field to present applications directly to the appropriate federal court for consideration.

S. 2402 would delete the authority currently possessed by all heads of federal agencies to approve (i)(1) applications, thereby centralizing application authority in a single agency, the Department of Justice, where it can be more effectively coordinated. Since 1976, only five applications for (i)(1) orders have been signed by non-Justice Department entities; this change will not, therefore, adversely affect federal agencies.

The revised (i)(1)(D) also clarifies existing law by explicitly providing that redisclosure can be made to those support personnel necessary to prepare for a criminal prosecution. This would not change existing practice.

Finally, the new (i)(1) provides that court orders may be granted by U.S. Magistrates as well as U.S. District Judges. Magistrates are now authorized to grant analogous applications such as those for search and arrest warrants.

Disclosure pursuant to formal law enforcement request (26 U.S.C. 6103(i)(2))

Section 4, Part 2. The revised § 6103(i)(2) clarifies existing law governing requests for non-return information. As amended, (i)(2) would permit requests to be made by

Justice Department officials in the field, as designated by the Attorney General, to avoid the necessity of routing all requests through Washington. It is anticipated that the Attorney General would authorize Assistant United States Attorneys and supervisory-level officials of investigative agencies to request non-return information, i.e., officials not directly involved in an investigation. In addition to the heads of agencies now authorized to request (i)(2) information, S. 2402 would grant similar authority to the fifteen Inspectors General whose mandate is to combat fraud, waste and abuse in federal programs.

The new (i)(2)(C) also authorizes these federal law enforcement officials to inquire whether a taxpayer filed a return for a given year and whether there is or has been a criminal investigation of the taxpayer. This will help avoid the waste of resources which has occurred where a court order is sought and obtained only to find that the taxpayer did not file a return for the year in question.

Finally, the revised (i)(2) would modify the factual showing required to support a disclosure of non-return information by substituting "the allegation of criminal conduct giving rise to the proceeding or investigation" for "the specific reason or reasons why such disclosure is or may be material to the proceeding or investigation." Like the (i)(1) court order requirement, a prosecutor cannot show the materiality of tax information to a case without access to the information sought.

IRS-initiated disclosure (26 U.S.C. 6103(i)(3))

Section 4, Part 3. S. 2402 proposes two improvements to the procedure by which IRS initiates reports of non-tax crime to law enforcement authorities. First, the new § 6103(i)(3) would make such reports mandatory rather than discretionary. Second, the new (i)(3)(B) provides that when the IRS refers a tax case to the Department of Justice, it must also refer any evidence it has of non-tax crimes committed by the taxpayer. The purpose of the non-disclosure rule is to encourage taxpayers to report their incomes fully and honestly; taxpayers who evade taxes should not benefit from a policy enacted to encourage honest reporting. The proposed section requires the IRS to disclose criminal information it uncovers except return information. Under the present act, IRS is not required to disclose the information [and the evidence at PSI's hearing disclosed that they do not]. This section eliminates the Catch-22 situation of requiring an agency to request information without ever knowing what information exists. It also requires IRS to alert the Justice Department to criminal information.

Admissibility of tax information (26 U.S.C. 6103(i)(4))

Section 4, Part 4. Finally, section 4 of the compromise bill would amend (i)(4) of § 6103 to provide that tax information is admissible in judicial and administrative proceedings like other evidence rather than pursuant to special rules. The bill also clarifies that tax information is admissible in proceedings "ancillary" to criminal proceedings, i.e., those arising from the same course of conduct and involving the same parties. Civil proceedings ancillary to criminal proceedings include civil forfeiture or damage actions which may be pursued in addition to or in lieu of criminal prosecution.

The amendments to (i)(4) also clarify that tax information may be disclosed to a defendant pursuant to the Jencks Act, discovery provisions of the Federal Rules of Criminal Procedure or other discovery requirments. This explicitly protects a defendant's Due Process rights and is consistent with current practice.

Emergency disclosure

Section 5, Part 1. S. 2402 would add three new paragraphs to § 6103(i). The new paragraph (i)(5) would permit IRS, in its discretion, to report to the appropriate federal agency any circumstances involving an imminent danger of physical injury to any person, serious property damage or flight from prosecution. This authority for disclosure in rare emergency situations is patterned on the similar provisions of the Financial Privacy Act of 1978 (12 U.S.C. 3414(b)) and, like the Financial Privacy Act, requires that all such disclosures be reported promptly to the appropriate federal district court.

Joint investigations

Section 5, Part 2. The new (i)(6) merely states that § 6103 does not preclude or prevent IRS from assisting or working jointly with federal law enforcement agencies in the investigation of non-tax crimes which may involve violations of federal tax laws. This does not change current law, but clarifies the law whch now discourages such cooperation by the vague and uncertain language in the act.

Disclosure to State and local authorities

Section 5, Part 3. S. 2402 also proposes a new (i)(7) authorizing carefully limited redisclosure of tax information to State and local law enforcement authorities. This limited redisclosure would be permitted only as to information already obtained by federal law enforcement officials for a federal non-tax criminal investigation. If such information reflects a State felony violation, the federal official obtaining access would be authorized to go back to court and seek an order authorizing redisclosure to the appropriate State attorney general or district attorney exclusively for use in the investigation or prosecution of that State felony violation. Like other persons receiving tax information, the State attorneys general and district attorneys receiving tax information under (i)(7) would be subject to civil and criminal sanctions for any unauthorized use.

Disclosure pursuant to mutual assistance treaties

Section 6. S. 2402 would amend § 6103(k)(4) to permit disclosures to foreign governments pursuant to mutual assistance treaties for use in non-tax criminal matters such as narcotics trafficking, thereby making it possible for federal officials to obtain reciprocal disclosure of foreign tax information. Such treaties, of course, must be ratified by the Senate. To further regulate this foreign access to tax information, the amended (k)(4) would require entry of an order by a U.S. district court, similar to that required by § 6103(i)(1), before a disclosure could be made. Paragraph (k)(4) presently authorizes similar disclosures to foreign governments for tax use pursuant to international tax conventions.

Criminal penalties

Section 7 would amend the criminal provision of the Internal Revenue Code; 26 U.S.C. 7213, to create an affirmative defense to prosecution where the disclosure of tax information in question was made pursuant to a good faith but erroneous interpretation of the law.

The new subsection would make it clear to federal employees that they need not fear criminal prosecution if they proceed reasonably and in good faith. Actually, this makes no practical change in existing law which requires a "willfull" violation to sustain a conviction. It would, however, reduce the extreme chilling effect which present law has on legitimate disclosures.

Civil remedy

Section 8 would amend the civil remedy section of the Internal Revenue Code, 26 U.S.C. 7217, to make federal agencies, rather than individual federal employees, the defendants in suits alleging unauthorized disclosures of tax information. This change would conform § 7217 to the Financial Privacy Act of 1978 (12 U.S.C. 3417) and the Administration's proposed Tort Claims Act amendments.

Under present law, civil suits may be filed against both the federal agency and the employee involved. The creates a potential conflict of interest requiring retention of private counsel to represent the employee. Moreover, it is unduly harsh to place federal employees who work with tax information regularly in the position of risking financial ruin daily for any mistaken disclosure.

Of course, federal employees would continue to be subject to administrative sanctions, including dismissal, for any negligent disclosure as well as criminal prosecution for any willful, corrupt or malicious abuse of tax information.

Conforming amendment

Section 9. The final section of the compromise bill is a technical conforming amendment to make the remaining provisions of § 6103 consistent with the new two-part definition of tax-related data held by IRS.

Disclosure Provisions
Comparison of Existing Law to Nunn Proposal

26 USC 6103 Existing Law	NUNN Proposal	Comments
(a) General Rule--"Returns" and "return information shall be confidential, and no person who had had access to returns or return information shall disclose the returns or information, except as authorized in §6103.	Change in nomenclature to reflect new terms "return information" and "non-return information" vice "returns" and "return information."	
(b) Definitions		
(1) Return--Tax or information return, declaration or estimated tax or claim for refund, or claim for refund, or amending or supplement thereto, including supporting schedules, attachments, or lists which are supplemental to, or part of, the filed return.	(1) Return information--Includes tax returns and supporting documentation now covered under "return" and "any information provided by or on behalf of an individual taxpayer [including natural persons or corporatives, partnership, association, union or other entity consisting of no more than 2 owners, shareholders, partners, or members] to whom such information relates." (See (b)(3) below.)	The 3 existing definitions are reduced to 2. DOJ must obtain an ex parte order to gain access to tax returns, supporting submissions, or any other information submitted to IRS with respect to an individual or a small corporation, partnership, association, union, or other entity made up of no more than two members. The records of a small corporation owned by a man and his wife, for example, will be protected by the court order provision. Records of a large corporation other than tax returns and other accompanying documents required by law to be supplied to IRS (in which privacy expectations are less because a number of persons have access to the information) would not be covered by a court order but would require a formal request from the DOJ to IRS. Information which does not identify a particular taxpayer, such as statistical data and rulings which do not identify the taxpayer, may be disclosed without a court order.
(2) Return Information--A taxpayer's identity; the nature, source or amount of his income, payments, receipts, deductions, exemptions, credits assets, liabilities, net worth, tax liability, tax withheld, deficiencies, overassessments, or tax payments; whether the taxpayer's return was, is being, or will be examined or subject to investigation or processing; any other data received, recorded, prepared, or collected by, or furnished to a determination of tax liability; any written determination, or any background file document relating to such determination, which is not open for public inspection.	(2) Non-Return Information--Any other information in possession of IRS except data in a form which cannot be used to identify, directly or indirectly, a particular taxpayer.	

26 USC 6103 Existing Law	NUNN Proposal	Comments
(3) Taxpayer return information--Return information (as in (2)) which is filed with, or furnished to, IRS by or on behalf of the taxpayer or to whom such information relates.	(3) Individual Taxpayer--Any natural person or a corporation, partnership, association, union, or other entity consisting of no more than 2 owners, shareholders, partners, or members.	Carter administration and other witnesses advocated keeping the books and records of small corporations, etc., within the court order provision since these usually are, for all practical purposes, owned by a single individual, who has an expectation that these records will remain private. In the case of larger corporations, the courts have made clear that no such privacy expectation is present.
(i) Disclosure for administration of Federal laws Federal laws not relating to tax administration. (1) Non-tax criminal investigation--	(1) Disclosure of return information	
(A) Information from taxpayer--Upon grant of an ex parte order by a Federal district court judge, a return or taxpayer return information shall be open, but only to the extent necessary as provided in the order, to officers or employees of a Federal agency who are personally and directly engaged in --and solely for their use in--preparation of any administrative or judicial proceeding (or investigation which may result in such a proceeding) pertaining to the enforcement of a specifically designated Federal criminal statute	(A) Return information shall be disclosed, pursuant to an ex parte order of a federal district court judge or magistrate, to officers and employees of the Justice Department who are personally and directly engaged in and solely for their use in preparation for any administrative, judicial, or grand jury proceeding (or investigation which may result in such a proceeding) pertaining to the enforcement of a specifically designated federal criminal statute (not involving tax administration). The order may provide for continuous disclosure if justified under subparagraph (B)(iii) [i.e., there is reasonable cause to believe the information may be relevant to a matter relating to commission of a criminal act].	Disclosure of return information would be permitted only to Justice Department personnel, not to those of other federal agencies as now permitted, and only for use in a criminal proceeding or investigation. This provides an additional check on the appropriateness and legality of disclosure. Magistrates, who may issue search warrants, would be allowed to issue ex parte disclosure orders as well as district judges. The present statute had a privision which included return information which has been loosely interpreted to cover taxpayer books and records, accountants' books and records, corporate records, third-party interviews, tips from other agencies and other material by law to provide IRS. Thus, the present act had the unfortunate result of putting IRS in the position of discovering bribery, embezzlement, union payoffs, etc. in financial records of organizations but not being able to turn it over or tell the Justice Department about it.

26 USC 6103 Existing Law	NUNN Proposal	Comments
(B) Application for order--The head of any Federal agency described in (A) or, if the Justice Department, the AG, Deputy AG, or Assistant AG, may authorize an application for an ex parte order.	(B) Application for order--The Attorney General, Deputy AG, an Assistant AG, a United States Attorney, or the Attorney-in-charge of a Criminal Division Organized Crime Strike Force may authorize an application for an ex parte order.	Applications for ex parte orders could be made only by certain DOJ officials, not by officials of other agencies. This is an additional privacy safeguard not in existing law.
The judge may grant the order if he determines on the basis of facts submitted by the applicant that--	The judge or magistrate may grant the order if he determines on the basis of facts submitted that--	The existing standards require DOJ to describe with specificity tax information that its attorneys have never seen. This leads to a "catch-22" situation. The proposed changes would establish standards similar to those now required under the federal wire tap statutes. While they would eliminate the "catch-22" aspects, they are high enough to protect against indiscriminate violations of individual privacy.
(i) there is reasonable cause to believe, based on information believed to be reliable, that a specific criminal act has been committed;	(i) [no change]	
(ii) there is reason to believe that such return or return information is probative evidence of a matter in issue related to the commission of such criminal act; and	(ii) the information is sought exclusively for use in a federal criminal investigation or proceeding concerning such act; and	The proposed standard is more reasonable with the added safeguard of prosecutorial intervention. The main criticism of the present standard was that it was impossible to meet. Therefore, no one used it.
(iii) the information sought to be disclosed cannot reasonably be obtained from any other source, unless the information constitutes the most probative evidence of a matter in issue relating to the commission of such criminal act.	(iii) there is reasonable cause to believe that the information may be relevant to a matter relating to the commission of such criminal act.	Also we've eliminated the third requirement that the Government prove the financial information cannot be obtained from any other source. The fact is that the financial information is "available" elsewhere but that the Government would have to completely reconstruct a taxpayer's bank records to duplicate the information on the return. This third requirement of the present act also requires the Government to prove that the tax return was the most probative evidence of the crime to be proven. Since this section deals only with non-tax crimes, the tax return itself would never be the most probative evidence of the crime. Only the actual financial record would qualify. Thus an impossible standard would be deleted.
However, IRS shall not disclose any return or return information if it determines and certifies to the court that such disclosure would identify a confidential informant or seriously impair a civil or criminal tax investigation.	No change.	

26 USC §6103 Existing Law	NUNN Proposal	Comments
No similar provision.	(C) Duty of IRS--IRS shall disclose to the appropriate Justice Department attorney such information ordered disclosed as soon as practicable following receipt of the ex parte order.	Witnesses testified that even when an order is obtained under existing §6103, IRS has taken inordinate time to comply, even to the point of jeopardizing criminal trials. This new provision would remedy those delays.
Further disclosure is governed by (i)(1)(A) above.	(D) Further disclosure--The government attorney may further disclose return information to such other federal government personnel or witness as he deems necessary to assist him in a criminal investigation or in preparation for the administrative, judicial or grand jury proceeding upon which the ex parte order is based.	Essentially, there would be no change in further disclosure as a practical matter. This language is similar to that already contained in Rule 6(c) of the Federal Rules of Criminal Procedure, regarding the release of secret grand jury evidence.
(2) Return information other than taxpayer return information--Upon written request by agency heads authorized to apply for ex parte order [para. (1)(A)], information supplied by third parties (i.e., return information not supplied by or on behalf of a taxpayer) shall be disclosed to officers and employees of such agency personally and directly engaged in, and solely for their use in, preparation for any administrative or judicial proceeding (or investigation which may result in such a proceeding).	(2) Disclosure of Nonreturn information. (A) Upon written request from the head of a federal agency, the Inspector General thereof, or the Attorney General or his designee in the case of the Justice Department, the IRS shall disclose nonreturn information as soon as practicable to officers and employees of such agency personally and directly engaged in, and solely for their sue in preparation for any administrative, judicial, or grand jury proceeding (or investigation which may result in such a proceeding) as described in paragraph (1)(A).	The procedures for requesting nonreturn information would not be altered substantially. However, since the definitions would be changed, more information--such as corporate records, third party records, and witness interviews--could be produced pursuant to written request rather than by court order than is the case under existing law.

26 USC §6103 Existing Law	NUNN Proposal	Comments
Such written request shall set forth--	Such written request shall set forth--	
(A) the name and address of the taxpayer;	(i) the name and address of the taxpayer;	
(B) taxable period(s) to which the return information relates;	(ii) the taxable period(s) to which the nonreturn information relates;	
(C) the statutory authority under which the proceeding or investigation is being conducted; and	(iii) the statutory authority under which the proceeding or investigation is being conducted, and	
(D) the specific reason(s) why such disclosure is or may be material to the proceeding or investigation.	(iv) allegations of criminal conduct giving role to the proceeding or investigation.	Since it is DOJ and not IRS which must determine if evidence is material to a criminal proceeding or investigation, the change would require DOJ merely to cite the conduct which gave rise to the request.
However, IRS shall not disclose any return or return information if it determines that such disclosure would identify a confidential informant or seriously impair a civil or criminal tax investigation. The name and address of a taxpayer may be disclosed under this paragraph.	No Change.	
No specific provision on further disclosure (see(i)(2) above).	(B) Further disclosure--The agency head, an I.G., or the AG or his designce may further disclose nonreturn information to such federal personnel or witness as he deems necessary to assist him in preparation for the administrative, judicial, or grand jury proceeding upon which the request is based.	There would be no substantial change in further disclosure except permit disclosure to witnesses, who often must be shown evidence during an investigation or in preparation for a criminal proceeding. This is the same procedure now in effect pursuant to Rule 6(e), Federal Rules of Criminal Procedure concerning the disclosure of secret grand jury evidence.

26 USC §6103 Existing Law	NUNN Proposal	Comments
Under paragraph (i)(1), taxpayer identity information is considered to be taxpayer return information and subject to disclosure only by grant of an ex parte order. However, under paragraph (i)(2), taxpayer identity information may be disclosed in connection with the disclosure, pursuant to written request, of return information other than that provided by or on behalf of a taxpayer (i.e., third-party information).	(C) For this purpose, the name, address and social security number of a taxpayer, whether a taxpayer filed a return for a given year or years, and whether there is or has been a criminal investigation of a taxpayer shall be treated as nonreturn information.	Our section makes it clear that taxpayer identification information is available upon written request of the attorney for the government. This avoids problems such as those faced by law enforcement officers when trying to return stolen property according to social security numbers and IRS won't provide the information under the present act.
(3) Disclosure of return information concerning possible criminal activities--IRS may disclose in writing return information (other than that provided by or on behalf of a taxpayer) which may constitute evidence of a violation of Federal criminal laws to the extent necessary to apprise the head of the appropriate Federal agency charged with enforcing such laws. The name and address of a taxpayer may be disclosed, even though supplied by the taxpayer, if there is thid-party return information that may constitute evidence of a Federal crime.	(3) Secretary's duty to disclose nonreturn criminal information. (A) The IRS shall disclose, as soon as practicable and in writing, nonreturn information which may constitute evidence of a violation of federal criminal laws to the extent necessary to apprise the head of the appropriate federal agency or his designee charged with the responsibility for enforcing such laws. For this purpose, the name and address of the taxpayer shall be treated as nonreturn information.	Present law merely permits IRS to disclose third-party criminal information to DOJ. The change would put an affirmative burden on IRS to carry out every citizens basic duty to report evidence of crime, except where the information is return information. Our section requires the IRS to disclose criminal information it uncovers except anything listed on the tax return itself and accompanying records. Under the present act IRS is not required to disclose the information [and the evidence at the PSI hearing disclosed that they didn't]. The tax return would still be inviolate except via court order. This section eliminates the "catch-22" situation of requiring an agency to request information without ever knowing what information exists. This section also would require IRS to alert the Justice Department to criminal information.

26 USC s6103 Existing Law	NUNN Proposal	Comments
No similar provision.	(B) In addition to the above disclosures, whenever IRS recommends to DOJ a prosecution for tax law violation, it shall furnish to DOJ any return or nonreturn information reviewed, developed, or obtained during the tax investigation which may constitute evidence of a violation of federal criminal laws.	Once IRS has recommended a tax prosecution to DOJ, it can disclose tax information relating to the case. This minor alteration would only allow IRS, after it has recommended a tax case to DOJ for prosecution, the ability to give DOJ all information associated with that case.
IRS shall not disclose any return or return information if it determines that such disclosure would identify a confidential informant or seriously impair a civil or criminal tax investigation.	(C) However, IRS may decline to disclose any information under the above paragraphs if it determines that such disclosure would identify a confidential informant or seriously impair a civil or criminal tax investigation.	No change in substance.
No similar provision.	(4) Use in judicial or administrative proceeding--Any information obtained under paragraphs (1), (2), or (3) may be entered into evidence in accordance with the Federal Rules of Evidence or other applicable law in any administrative, judicial, or grand jury proceeding pertaining to the enforcement of a specifically designated federal criminal statute (not including tax administration) or any ancillary civil proceeding to which the United States or any agency thereof is a party.	This section codifies the commonly accepted rise of tax returns obtained pursuant to 6103 in federal courts according to the appropriate rules evidence. This section would also provide a mechanism to transfer information concerning federal civil litigation to the appropriate federal authority. Under the present act, no such provision exists. GAO found, for instance, that the Government under the present act lost federal civil cases of substantial size because it could not obtain information from IRS. This section would provide a mechanism to transfer information in serious civil cases such as civil rights, anti-trust and fraud cases which an ancillary to a criminal proceeding.

Chairman RANGEL. I would agree with you, Senator, and I do hope as I said earlier that our staffs can get together and try to get answers to some of these unanswered questions. I guess the framework in which we are dealing is that there are many people that believe that the Internal Revenue Service should not be a general law enforcement agency. You do not have any problem with it being that as long as the goal is to indict and convict criminals? You would have IRS be a cooperative part of general Federal law enforcement efforts—you do not have a problem with that?

Senator NUNN. I think that when the IRS comes across evidence of a nontax crime that information should basically be made available to the Justice Department, subject to the privacy of the Tax Reform Act itself.

Chairman RANGEL. If you do not know what is there, then you cannot ask for it. I am asking if IRS should volunteer and give it as a part of effective law enforcement. We have to define what we are really talking about. You would not have a problem with that?

Senator NUNN. The way I would state it is for instance right now if the IRS comes across evidence of an impending murder, a threat to the life of even the President of the United States, they cannot turn over this information if it comes from a tax return, and I think the American people would be repelled by that. I think the IRS would violate the law now if they——

Chairman RANGEL. The example you gave from your testimony was going through people's garbage and finding evidence, and that is different than an attempt at assassination of the leader of the free world.

Senator NUNN. I think it is absurd for the IRS to have access from a garbage search that was legal and which indicates narcotics violations and not be able to turn that over to the Justice Department.

Chairman RANGEL. I guess we can agree that it is a subjective determination as to the importance of the evidence. But you do not have a problem that in the course of its operation and collecting taxes, if IRS does indeed find information that could be criminal, that they turn it over to the appropriate agency?

Senator NUNN. That is correct.

Chairman RANGEL. The language you use, that law-abiding taxpayers can rest assured that the information supplied will not hurt them, of course often is used for those people who take advantage of the fifth amendment—that if you have nothing to hide then certainly you should answer the questions. I guess I will go along with you—even though a lot of people believe that they are hard-working and law-abiding, which again certainly is subjective. What bothers me is that you say that the only people that need to fear this legislation are narcotics traffickers and organized-crime figures and white-collar criminals who are cheating other taxpayers by not paying their fair share. As a former prosecutor of those accused of violating the Federal narcotics laws, I do not have a problem with that, except I do not think that your proposed legislation is really that tight—that we really are going after those who are involved in narcotic transactions, 1, and 2, that we have outlined what would be considered organized crime as opposed to just individual criminals. Because to the hard-working, law-abiding taxpayer, he or she may not be concerned about a DEA investigation or an FBI investigation or any law enforcement investigation. But I get a feeling that no matter how law-abiding you are or how hard you work, when you hear that the Internal Revenue Service is investigating, there is an appearance of an awesome, overwhelming power there that if they concentrate on you long enough, they can get an indictment. You use the magic words that you do not want to make the job easy for the prosecutor. Did you mean that, you believe as I do that the prosecutor could just target an individual and go to IRS and say he is the target of an investigation, and we cannot get enough evidence to convict but we hope you can help us find something to convict him?

Senator NUNN. For the prosecutor to be able to do that he has to show basically the same thing he would have to show to get a wiretap, in order to get access to that tax return. We change the method of responsibility regarding nontaxpayer supplied information. When they come across information not part of the tax return, they would have a duty to make the information available if it indicates another crime. The only way the prosecutor could get that return under our provision would be to go to court and show essentially the same thing you would have to show to get a wiretap. I do not think that privacy is any greater than the privacy attached to our telephones.

Chairman RANGEL. That is a problem. I do not know what we volunteer when we have a telephone installed. It is my understanding, however, that one of the greatest threats that we have to the current Federal tax system is the fact that it is voluntary and that so many people are now believing that it is OK to evade the law and to evade and avoid taxes. You are asking now for information that taxpayers give on a voluntary basis. Who gives all of this information? And now you are saying to a hard-working, law-abiding citizen, that if in the course of an investigation one law enforcement agency believes that you are guilty but has not sufficient evidence to even indict you, that we can now call upon the agency that has collected information that you have voluntarily given them to see whether or not they can reach that objective?

Senator NUNN. Mr. Chairman, that is the present law. The only problem is the present law has such a distorted definition of how you go about getting a court order. You set up a completely impossible situation. And you have just described the present law. But again, what we are doing is saying that the prosecutor would have to go to court to get this tax return, they would have to show essentially the same thing they would have to show for a wiretap. I do not think that is an abuse of anyone's right of privacy. You have got a court standing in between here, and I think that the American people, frankly, Mr. Chairman, are concerned about that privacy when it comes to being somewhat safe on the street from people who are seeking narcotics. I think the older people are beginning to feel they cannot leave their homes and apartments because of abuse on the streets. I think this includes some degree of safety in one's person and one's property, and we are virtually becoming, particularly in the inner cities, we are virtually becoming prisoners of people who are involved in narcotics traffic. I think the American people have a broader expectation of law enforcement than law enforcement is capable of delivering.

Chairman RANGEL. I would agree with you, especially in the cities, that people are fearful of the results of heavy drug addiction and the crimes related to it. I cannot go to a town hall meeting, a church or synagogue that people are not asking for stricter laws and longer prison terms. If it affects their families or people they know, they say they were not talking about those people, they were talking about the others. As long as I am not being harassed I would want a stricter interpretation of the law. I just do not see where you restrict this legislation to that dirty, filthy, drug-pushing person.

Senator NUNN. It would include murderers and pornographers, also. It would include white-collar criminals——

Chairman RANGEL. I do not see who it excludes, Senator.

Senator NUNN. It does not exclude a criminal violator who the IRS has evidence has committed a crime from only the tax return. Would you want to exclude child pornographers? You tell me who you want to exclude and I will tell you whether it excludes it or not.

Chairman RANGEL. I would say that a criminal is one that has been convicted. You are using the term as somebody who may be convicted with the cooperation of the IRS.

Senator NUNN. Are you saying that we should not have any cooperation with the IRS with law enforcement until the conviction has already occurred?

Chairman RANGEL. No.

Senator NUNN. Then we have got an impotent agency, because once the conviction has occurred, there is no need to have cooperation.

Chairman RANGEL. You were referring to all the people about whom IRS could cooperate with the Justice Department as already being determined as drug traffickers and organized crime figures and that they were criminals. We do not have any problem with that, of course. Like you said, who needs it after they are convicted. But there are a lot of people who are innocent who have been accused of crimes, and they are not criminals unless convicted.

Senator NUNN. There is nothing in this that shortcuts what has to occur before conviction. The Justice Department has to have a jury, a conviction, and go through the appellate process. This is talking about evidence of those type crimes.

Chairman RANGEL. Evidence that the proposed target volunteers to the Internal Revenue Service?

Senator NUNN. Not necessarily. There are two dimensions of this. One is the tax return itself. Frankly, that is the least important provision here. That is what the taxpayer supplies. We are providing a court order for that, no other way they can get a tax return except with the court order showing the same kind of burden that has to be shown for a wiretap. The evidence the Internal Revenue Service develops themselves, for instance the garbage can search, I do not believe that that kind of evidence should be protected under some strained interpretation of privacy. I think that is taking privacy to its ultimate absurdity.

Chairman RANGEL. Mr. Pickle.

Mr. PICKLE. Senator, you observed that for the past 7 years the Internal Revenue Service has primarily limited itself to tax administration rather than any aspect of nontax law enforcement. I think that is a correct observation. I also would observe that we are probably letting a lot of criminals, racketeers and narcotic traffickers, get away with obvious violations. Now, the law says that if Justice has information that this is happening, they can go to court and get a court order. They can pursue it. And we are advised on this committee that each time the Justice Department has asked for such a court order, they have been able to get it. First, is that so? Is there any difficulty getting a court order?

Senator NUNN. Congressman Pickle, the information we have from the prosecutor is that, first of all, they don't request the court orders in 99 percent of the cases because they are in a catch-22 situation. They virtually have to know what is in the tax return in order to make the request. So, it is probably correct that they do get court orders most of the time when they request it.

The problem is in the area where they don't make requests because they can't show the very stringent burden.

In effect, the Justice Department now has to almost already have the information in order to request it under the court order.

There have been very few cases where the court order has been turned down, but there have been very few cases where it has been requested.

Mr. PICKLE. In 99 percent of the cases, a court order has not been requested?

Senator NUNN. That is the information I have. Those 99 percent figures are my own subjective judgment, but that is based on the information that I have before our committee, as well as the FBI and DEA. We have a prosecutor from Texas who just testified and went through tremendous detail.

All this is available. We will have our staff give it to you showing how difficult it is to get a court order. He basically said he does not seek that kind of court order because it is just about impossible.

Mr. PICKLE. If the figure is anywhere near 99 percent, then the court order procedure is not effective at all.

Senator NUNN. That would be my feeling.

Mr. PICKLE. So we must do or should do something else. The question is, Can we correct this deficiency under the present law or do we need a change in the statute as you have proposed?

Senator NUNN. Congressman Pickle, I think that certain changes have already been made by the Internal Revenue Service in the last couple of years under both Carter and Reagan moving in the right direction. So there are some things that can be done short of changing the law, but in order to really correct the problem, I think the law has to be changed.

Mr. PICKLE. Is it your suggestion that if the Internal Revenue Service sees evidence that is obviously questionable that it should turn the information over to the Justice Department and let it make some kind of appraisal of that evidence in order that justice could then ask for a court order?

Senator NUNN. Well, that would only be on nontax returns. On tax returns, they could not do that unless there was an emergency involving persons or property, in which case we would put that affirmative burden on the IRS. We would make them then go to court to justify it.

But on nontax return information, we do put an affirmative burden on the Internal Revenue Service to turn that over to the Justice Department where it indicates to them a nontax crime.

Mr. **Pickle**. It seems to me that we need to make improvements either in the present law or along the line you suggest because there is a gap which, in effect, results in no prosecution. People feel then that they don't have to worry.

So, it seems to me that we must either tighten up our present procedure or pass some kind of legislation such as you are recommending.

Senator **Nunn**. I think that is right, Mr. Chairman, or either give up on high-level narcotics dealers because I know Congressman Rangel has been a prosecutor and he knows this better than I do by far, but they don't usually touch the narcotics. They always touch the money, and that is why IRS has to be brought into this.

I don't say that our procedure here is locked in concrete. I don't say that there can't be improvements made. I don't submit, Mr. Chairman, that there can't be ways to strengthen what we propose to insure that the goals you are anxious to see preserved are preserved.

What I am saying is that the present situation has to be changed. The General Accounting Office has done a thorough study of this and has made their own recommendations. I would also submit, Mr. Chairman, that if the staff could carefully study the GAO recommendations, I think that would be enormously helpful, too.

Chairman **Rangel**. Mr. Crane?

Mr. **Crane**. Thank you, Mr. Chairman.

I want to welcome the distinguished Senator to the committee, and second, congratulate him for the work that he has invested in this proposed legislation.

I have a couple of questions, and I am speaking as one who is naive on much of this.

You made reference to IRS agents on page 6 of your testimony. They found evidence of massive embezzlements when they audited a labor union's records, but they could not report this information to Justice.

Under the special enforcement program of IRS, did they not investigate that particular case or had these embezzlers simply reported all of the money they took in through embezzlement and paid taxes on it, and, therefore, in the eyes of IRS, had committed no crime?

Senator **Nunn**. I cannot give you the answer on that. We can supply it for the record, but I think the point is they did not pursue the embezzlement. They may have pursued the tax evasion if there was tax evasion, but my vague recollection, subject to correction of the record, is that there was no tax crime. There had been taxes paid on this, but there was an embezzlement crime that had not been pursued. That is my vague recollection.

Mr. **Crane**. Was that also true in the case of the policeman who took the bribe?

26 USC §6103 Existing Law	NUNN Proposal	Comments
No similar provisions	Any such information may be disclosed to the extent required by order of a court pursuant to 18 USC 3500 or Rule 16 of the federal Rules of Criminal Procedure, or other applicable discovery requirements, such court being authorized in the issuance of such order to give due consideration to congressional policy favoring the confidentiality of return and nonreturn information as set forth in this title. However, any information obtained under paragraphs (1), (2), or (3) shall not be admitted into evidence in such proceeding if IRS determines and notifies the AG or designee or the head of such agency that such admission would identify a confidential informant or seriously impair a civil or criminal tax investigation, unless the court shall otherwise direct such disclosure.	
No similar provision.	(5) Emergency circumstances--Under emergency circumstances involving an imminent danger of physical injury to any person, serious physical damage to property, or flight from prosecution, IRS may disclose information, including return information, to the extent necessary to apprise the appropriate federal agency of such emergency. As soon as practicable thereafter, IRS shall notify DOJ of this action, and DOJ shall thereupon notify the appropriate federal district court or magistrate of the disclosure.	This section allows IRS to disclose any information to the appropriate agency in circumstances where a threat exists of injury to a person, serious damage to property, or flight from prosecution. This obviates problems that exist under the present law where even threats of assassination couldn't be disclosed without elaborate and time-consuming procedures. This section requires that after the emergency disclosure, the Government notify the appropriate court of the disclosure.

26 USC §6103 Existing Law	NUNN Proposal	Comments
No similar provisions.	(6) Assistance of IRS in joint tax and non-tax investigations--No portion of §6103 shall be interpreted to preclude or prevent IRS from assisting any other federal investigative agency in investigations of criminal matters which may lead to income tax violations, or from investigating or gathering relevant information concerning persons involved in such criminal activities.	This section makes it clear on the face of the statute that IRS is free to work jointly with other government agencies in combating crime. This is to obviate the need to process a Title 26 Grand Jury request simply to obtain the assistance of IRS. Hearing testimony revealed that the Grand Jury request process took upwards of one year just to obtain the services of IRS in a criminal case.
	(7) Disclosure to State authority upon certification of evidence of a State felone violation--the official to whom disclosure has been made may apply to a district court for an ex parte order to further disclose to a State Attorney General or district attorney any return or nonreturn information that is relevant to a violation of a State felony statute. The application shall set forth the name and address of the taxpayer, the relevant taxable period(s), the State felong violation and statute, and a description of the information sought to be disclosed.	This section gives the government a mechanism to provide evidence of state crimes to the appropriate authorities. The present act contained no such provision. This section provides for a court-authorized procedure to give evidence of state crimes to state authorities. Under the present act, for instance, evidence of bribing a policeman in the hands of IRS could not be given to the appropriate state authorities. Our revision provides a mechanism to accomplish this which includes a court order as a privacy safeguard.

26 USC §6103 Existing Law	NUNN Proposal	Comments
No similar provision.	The order for discloure to State authorities may be granted if the judge or magistrate finds on the facts submitted that— (A) there is reasonable cause to believe, based on information believed to be reliable, that a specific state felong violation has occurred; and (B there is reasonable cause to believe that the information may be relevant to a matter relating to the commission of such violation.	
No similar provisions.	(k)(4) Disclosure to competent authority under international convention--Return or non-return information may be disclosed to competent authority of a foreign government which has a tax convention, mutual assistance treaty, or other convention relating to the exchange of tax information with the U.S. but only to the terms of the agreement. Disclosure of return or nonreturn information sought pursuant to a treaty or convention for use in non-tax criminal matters may be made only after a U.S. district judge or magistrate issued an ex parte order that there is-- (A) reasonable cause to believe that the information may be relevant to a matter of a specific criminal act that has been committed or is being committed against the laws of the foreign country, and (B) that the information is sought exclusively for us in such country's criminal investigation or proceeding concerning criminal act.	This section creates a mechanism to allow the Government to perform according to mutual assistance treaties it has entered into with foreign countries to exchange criminal evidence. Under the present act, IRS refused to give criminal evidence to the Justice Department so that it could comply with this country's mutual assistance treaties.

26 USC §6103 Existing Law	NUNN Proposal (Criminal Penalty for Disclosure)	Comments
(a)(1) It shall be unlawful for any present or former officer or employee of the federal government to willfully disclose any return or return information except as authorized in 26 USC 6103. A violation is punishable by a fine not exceeding $5,000 or 5 years in prison, or both, together with the costs of prosecution, and any person convicted of a violation shall be discharged from Government employ.	No change.	
	(d) It shall be an affirmative defense that such disclosure of return or nonreturn information resulted from a good faith, but erroneous, interpretation of section 6103 while a federal employee was acting within the scope of his employment.	IRS agents testified that section 6103 is very technical and detailed, and that IRS' interpretations of the section have been confusing to them. Therefore, rather risk violating 7213, which contains no good faith defense, they are "gun shy" and reluctant to disclose criminal evidence even when, as a technical, they are permitted to do so. Therefore, a good faith defense would be added to 26 USC 7213.

26 USC 7217 Existing Law	NUNN Proposal (Civil Penalties for Disclosures)	Comments
(a) General rule--Whenever any person knowingly, or by reason of negligence, discloses a return or return information in violation of section 6103, the taxpayer may bring a civil action for damages against such person.	(a) General rule--Whenever any federal employee knowingly, or by reason of negligence, discloses return or nonreturn information in violation of section 6103, the taxpayer may bring a civil action for damages exclusively against the agency employing that employee. Whenever any person other than a federal employee discloses return or nonreturn information in violation of section 6103, the taxpayer may bring a civil action directly against such person.	The change shifts liability for damages for authorized disclosure in the case of a federal employee from the individual employee to the Government.

Senator NUNN. That is right. He paid taxes on it, and as of a year ago he was still on the police force.

Mr. CRANE. Now, in turning to the court order mechanism, and looking at the liberalization in H.R. 1502 and Senate bill 1891, why, in your estimation, is liberalization required for getting at tax records? What is the inherent deficiency, for example, of a Federal district court judge providing such a court order to get at tax records?

Senator NUNN. Congressman Crane, I will submit for the record a comparison of existing law with this proposal, but to make a long story short, the degree of particularity—and on page 3 it goes into this—right now what has to happen in order to get a court order, first of all, you have to show, No. 1, that there is reasonable cause to believe, based on information you believe to be reliable, that a specific criminal act has been committed. That is No. 1.

No. 2, there is reason to believe that such return or return information is probative evidence in a matter of an issue related to commission of such a criminal act.

Three, the information sought to be disclosed would not be reasonably obtained from any other source unless the information constitutes the most probative evidence of the commission of such criminal act.

No. 3 is the problem. First of all, a tax return is never the most probative evidence. There is also some other evidence in front of that.

The other catch 22 is that you have to show that you can't reasonably obtain that from any other source. Until you get the information, you don't know what the other source might be. So, they are just in an impossible situation.

Those are the provisions we are changing so that we would go more to a provision that says, what we say in No. 1—there would be no change.

First of all, you would have to have reasonable cause to believe, based on information believed to be reliable, that a specific criminal act had been committed. That is No. 1. We would retain that.

Second, we would say the information is sought exclusively for use in a Federal criminal investigation or proceeding concerning such act.

Third, there is reasonable cause to believe that the information may be relevant to a matter relating to such commission of a criminal act. So, we are changing the standards in that respect for a court order.

Mr. CRANE. In the case of the trashcan incident, what was the basis of the court order permitting the law enforcement agents to have access to the records that had been picked up by IRS at that time?

Under the three provisions that you had cited——

Senator NUNN. First of all, it is my recollection under that that the Internal Revenue Service did not notify the Drug Enforcement Administration. The Drug Enforcement Administration found out through other sources that the IRS had this information. They asked for it. It was not asked for with a court order.

The Internal Revenue Service then said that they could not turn it over without a court order because it was encompassed in this taxpayer return information.

That is the distorted interpretation of the law, in my view. I think they went too far in interpreting even the existing law. I think they could have turned it over, but they did not.

Third, I assume that DEA did not either have time to go to the court and get an order or they could not meet the requirements of those three provisions with regard to that particular piece of trash information.

Mr. CRANE. Well, I thought in your testimony that you indicated that the prosecutor needed a court order. Did he not secure it in that instance?

Senator NUNN. Marty Steinberg, my chief counsel, would know the details better than I would.

Mr. STEINBERG. As I understand it, when the Justice Department needed information for an ongoing criminal proceeding, they could not obtain it in a timely fashion and they did not obtain it in a timely fashion. The proceeding was over before they could obtain the evidence they needed; that is, the trial.

Mr. CRANE. I am puzzled then as to the source of information that first was secured by IRS, or rather by DEA, if they were the ones investigating, that prompted them to even seek that tax information.

Is this a deficiency more in the realm of the lack of alacrity with which the bureaucracy works with existing mechanisms?

Senator NUNN. I frankly think that that example is more of an indictment of the bureaucratic framework and interpretation than the law itself. I think that interpretation was carrying much too far the existing law.

Mr. CRANE. I thank you. I have no further questions.

Chairman RANGEL. Mr. Jenkins?

Mr. JENKINS. Thank you, Mr. Chairman, and Senator.

I want to express my appreciation to you, Senator Nunn, for your diligent work in this area. I know from talking with you and from reading your previous remarks that you are greatly concerned that some of the existing interpretations of the law are proving to be a considerable hindrance to law enforcement agencies.

At the same time, this is a very tight rope that we are walking. We do want to protect the right to privacy under the Constitution and to make sure that the Internal Revenue Service is not turned into an agency that simply uses this information for wholesale investigations of people. I know that you don't intend to do that.

Let me ask you this: As I understand it, your proposal has a lesser standard for release of nonreturn information. Would there be an affirmative duty on the part of the IRS to disclose that information to the assistant U.S. attorney or U.S. attorney if it was felt that there was sufficient evidence to establish that there might be a crime involved?

Senator NUNN. In the provisions we have, we put a duty on the Internal Revenue Service. We say they shall disclose to the appropriate Justice Department attorney such information ordered to disclose as soon as practicable.

The Government attorney may further disclose return information to such other Federal Government personnel. In disclosure of nonreturn information, I think that is getting to what you are talking about.

Upon written request from the head of a Federal agency, the Inspector General thereof, or Attorney General or his designee in the case of the Justice Department, the IRS shall disclose nonreturn information as soon as practicable to the officers and employees of such agency personally and directly engaged in and solely for their use in preparation for any administrative, judicial, or grand jury proceeding or investigation.

The requirement for that information: It requires a written request. The request would state, first of all, the name and address of the taxpayer; second, the taxable period; third, the statutory authority under which the proceeding or investigation is being conducted; and fourth, the allegations of criminal conduct giving rise to the proceeding or investigation.

We basically loosen up the definition of the nonreturn information. That is the big change here rather than the procedure once it happens.

Right now the words in the definition of the existing statute, "taxpayer return information" and "tax return information" are so broad that they just sweep in almost everything into the court order category so we do restrict those definitions so that the court order category is not nearly as broad.

Mr. JENKINS. Let me see if I understand correctly.

Assuming that an audit was being performed by the IRS and the IRS agent came across certain information in books of the individual or entity that might indicate that a crime had been committed. What is the duty, if any, of the IRS agent at that point under your proposal?

Senator NUNN. If it is an individual's books or records that have been turned over by the taxpayer, they would still be subject to the court order.

Mr. JENKINS. I am talking about a field audit.

Senator NUNN. If it was information that was not under that definition, then the Internal Revenue Service would, if they thought it was a nontax crime, be required to turn it over to the Justice Department.

Mr. JENKINS. This concerns me somewhat, recognizing the wide dragnet effect of Federal conspiracy statutes. Suppose that an agent, in checking the books, discovered that there were huge amounts of money coming in from some enterprise that might appear legal, but which might, in fact, have some SEC violation or some mail fraud possibilities. At that point if he or she thought that this taxpayer might possibly be involved in some illegal activity, would it be an affirmative duty on their part at that point to contact the U.S. Attorney and reveal this information?

Senator NUNN. That would be, that is right. Now, they would not be making it public, but it would be turned over to the Justice Department.

The big changes here relating to nontax return information relate, first of all, to the definition which I alluded to. It is a narrow definition for what is required by the court order.

Second, the present law says the Internal Revenue Service may turn over that information. They have that authority now, but this is covered by saying "shall".

Mr. **Jenkins**. I suspect that many of the agents are so cautious now because of the civil and criminal penalties involved in the existing law.

Senator **Nunn**. That is because of an overinterpretation, yes, sir.

Mr. **Jenkins**. They are extremely reluctant to do what they could do under existing statute.

Senator **Nunn**. I think that is right.

Mr. **Jenkins**. I know that my intent would be the same as yours, that we don't broaden the law to the extent that we go beyond the scope of the Internal Revenue Service's function.

Senator **Nunn**. Congressman Jenkins, I know you are very concerned in this area. I would say that if there are certain crimes that the committee in its wisdom sees that should not be subject to this kind of turnover, that those could be specifically excluded in the provision.

Mr. **Jenkins**. That list might get quite broad. For example,there is a distinction between bribery, by a foreign country and a legitimate payment. That is causing a great deal of confusion now and would be one area that could cause some problems.

Of course, in my part of the country they already do this, you know. When you find a grocery selling a lot of sugar, sometimes it is suspected that someone might be making a little illegal whiskey. That already is a tax-related crime.

Senator **Nunn**. I thought all that had been cleared up in Georgia.

Mr. **Jenkins**. Only the good stuff is left.

Senator **Nunn**. I would agree with you. That whole area of bribery, even if you don't change the law at all, we have got real problems there. If there is enough confusion in that point that that ought to be excluded, I would certainly understand that.

Chairman **Rangel**. Mr. Moore?

Mr. **Moore**. Thank you, Mr. Chairman.

Senator, I appreciate your being here today. It seems to me that from the impressions I have from years of studying and then being involved in Government, that its first duty is to protect its citizens from attack from without its borders and, from internal disorders within its borders; and all other functions of Government—building bridges, schools, and all of that—is strictly secondary to this first and greatest duty.

It also seems to me that we are protecting and overprotecting criminals today far too much. It probably even gets as far as this area of confidentiality in tax matters, as you are testifying, this point that we may well be jeopardizing citizens at the risk of overprotecting criminals, thereby reducing or eliminating the success of that first governmental duty, protecting its citizens from internal disorders.

It appears to me that this overprotection of criminals is a very serious matter and something we ought to take a close, hard look at. Certainly I am going to do so in this limited area, as you have asked us to do.

You seem to have done a lot of work in this area, and according to the reading that I have done in some areas of protecting criminals, we seem to protect them more than some other notable democracies with longer histories of freedoms and fair trials.

I am wondering if you have done any comparative analyses with, say, Great Britain and their confidentiality of records, and what they have in the law and what they prescribe?

Senator NUNN. I have not, Congressman. I think it would be a useful bit of information to have. I would like to have it, but I do not have that.

Mr. MOORE. It seems to me also, as an observation, that the pendulum tends to swing to the pre-1976 situation and appears to have been——

Senator NUNN. It was wide open. I would in no way advocate going back to that.

Mr. MOORE. Then we passed the 1976 statute. It appears as we often do in Congress, we overreact, and we got ourselves too strict. Would it be fair to characterize your bill as moving back somewhere in between pre-1976 and where we are now?

Senator NUNN. I would say on a scale of zero to 10, and using the present law as 10 and using the pre-1976 law as zero, that this would be moving back somewhere around 4 or 5, in that nature.

I think it does retain the majority of the protections, probably as much as 60 or 70 percent of the protections of the 1976 law. In one way, it strengthens the 1976 law because it does say that only the Justice Department can request this information. The present law would permit any agency to make a request, but we do liberalize, of course, the definitions, and we also eliminate the Catch 22.

Mr. MOORE. In addressing that particular issue, it appears to me that your court ordered disclosure does not appear to be too great a change from what the law is now. It appears to me that where you are making the greatest change is in the proposed definitional changes in permitting disclosure of underlying books and records of corporations, associations, and partnerships.

Would you agree with that analysis?

Senator NUNN. I think that is right, and I would say to the committee that I struggled with this definition of what is a small business. I am ranking minority on the Small Business Committee, and I have never heard a precise definition. If the committee would like to expand that definition, I would welcome that.

I just never have known how to draw a line on what is a small business and what is a large business. It is easier to say individual proprietorship, but whether it ought to be two stockholders to have this court ordered protection on nonreturn information or whether it ought to be 25 is a matter of judgment. I do not profess much wisdom on that.

Mr. MOORE. There will be some here soon who are going to make the argument before this committee during the course of the hearings that if we in any way liberalize the present law, then that is going to discourage taxpayers from reporting to the government what their real income is.

I am asking you the question, based upon your experiences as the chairman of the subcommittee and how ranking minority member of that same committee, and where you have held hearings in this matter, can you imagine situations wherein a criminal would be honest with the IRS and dishonest in every other aspect of law?

Senator **Nunn**. I certainly cannot, Congressman Moore, and I would say to you that if you look at the growth of noncompliance with the tax laws, they have grown tremendously since 1976.

Now, I do not contend that the entire reason for that is the Tax Reform Act, but I think there is a growing disillusionment among American taxpayers, particularly average taxpayers who feel like they are being harassed by the Internal Revenue Service at the same time they are reading that $40 to $50 to $60 billion is being taken in through narcotics transactions in this country that is not being taxed.

So, I would think voluntary compliance would go up dramatically if the Internal Revenue Service proved that it had some effectiveness in cooperating with Justice in going after these high-level criminals.

All Internal Revenue Service people that I know have said over and over again that they had more voluntary compliance grow out of the successful IRS investigation of Al Capone than any other single instance.

So, I believe that if any case can be made—and that is the question—that there is a connection between the 1976 law and voluntary compliance, the case I think could be made much more successfully that the 1976 law has diluted voluntary compliance.

Mr. **Moore**. We have had other oversight hearings before the subcommittee on this problem of the underground economy, and we had them in the prior Congress, that showed that this is indeed a growing problem. What the reason for it is I am not sure anybody knows, but it is a growing problem. Tremendous sums of money are there that we should be collecting.

Is it your opinion that if we liberalize somewhat, such as your bill proposes, the release of taxpayer tax return information to other Federal agencies, that IRS might well receive back tax info uncovered in the course of their investigations.

Senator **Nunn**. That is certainly correct. That could happen, and I think what has happened now—this is an important subtlety that is hard to document, but I know it for a fact because I have talked to so many people; that is, that when you have the Internal Revenue Service not having any flow of information in the Justice Department, FBI, DEA, et cetera, what that inevitably involves is that the two-way street begins to work backward.

The FBI, DEA, and Justice are now probably at an all-time low turning information over to IRS relating to tax crimes. So, this is beginning to have a significant detrimental effect on tax collections themselves because IRS is not getting the flow of information from other law enforcement officials about tax evasion.

Now, perhaps that has changed somewhat in the last 2 years since we put the spotlight on this, and we think there have been certain internal changes in IRS which we consider positive, but that is a general description since 1976.

Mr. **Moore**. Thank you, sir.

Chairman **Rangel**. Mr. Duncan?

Mr. **Duncan**. Thank you, Mr. Chairman.

I want to thank the Senator and compliment you on your initiative in this bill, which I consider very, very important.

It seemed like we may be trying to complicate a situation that might be handled in an easier way. The way I understand it, under current law, when an Internal Revenue Special Agent runs across information of law violations, he is unable to disclose that information.

Why could not we simplify the entire matter by making it legal, in some way, that when the agent ran across the information of law violations, that he could disclose that information to one of his superiors or through the Department of Justice? Why could not we do that?

Senator NUNN. Well, that is the thrust of what we are trying to do.

Mr. DUNCAN. Well, it seems kind of complicated. Why couldn't we just simply do that?

Senator NUNN. Well, if you could figure out a way to do it, I would join you as cosponsor.

Mr. DUNCAN. It would take me about an hour to figure it out, if you will wait around.

Senator NUNN. Well, I would like to see it because I have been into this in great detail. To try to preserve the essential privacy and, at the same time, eliminate some of the absurdities of the present law, it dictates a complex legislation.

I regret it because I would like to deal with it in a very simple way, but I think if you try to deal with it in those terms, you will find that you have really repealed a lot more of the law than you want to and that because you have got to retain—for instance, we retain a court order for the tax returns and to retain that court order for the tax returns to be turned over requires some detailed drafting in terms of definitions, in terms of standards of proof and so forth.

I would not want to see the law rolled back to the pre-1976 standards where you had to have no court order whatsoever for turning over a tax return. I think that would be moving the pendulum back too far in the other direction.

Mr. DUNCAN. In your investigation, in how many cases, do you know, was needed information found elsewhere while the 6103 application was pending?

Senator NUNN. I have a list of examples here I would like to submit for the record, Mr. Chairman. In addition, we just had a prosecutor from Texas——

Mr. DUNCAN. Do you know how many nationwide?

Senator NUNN. I can submit all that for the record, but we have had bits and pieces. There has been no comprehensive survey that I know anything about.

We had DEA and the Justice Department. We asked them one Thursday or Friday to do a brief inventory for next week on how many cases they run into where this law precluded successful exchange, and they came up with a number. They came up with a multitude, but that was not a comprehensive and exhaustive list.

We found 70 examples in a 3-day period, but I think that is just scratching the surface.

Mr. DUNCAN. Do you know how many criminal nontax investigations with prosecutions had to be closed or that were lost by the Department of Justice because the Justice Department did not have access to the tax-related information?

Senator NUNN. I would have to ask Justice to supply that. I am not the best witness on that point.

Mr. DUNCAN. Did you cover that during your investigation?

Senator NUNN. We did. We asked the questions, and we never got definitive answers. We just get the impression that they have been numerous.

Mr. DUNCAN. Thank you very much.

Mr. CRANE. Will you yield for just one question?

Not being a lawyer, I can be excused for some naivete again in my questions.

If I were working for IRS and I found specific evidence of the commission of a major crime in the process of doing my investigation, but found in that investigation that no violation of our tax code existed—murder, for example—am I not an accomplice after the fact if I withhold that evidence, as a private citizen, from authorities, and, am I not potentially subject to prosecution?

I am thinking of the people at IRS who know, based upon their audits, that a crime occurred and yet have withheld that information.

Senator NUNN. I think an ordinary citizen placed in that position would be violating a law and would become an accomplice. I think that the Tax Reform Act of 1976 would clearly exclude IRS agents from that.

Mr. CRANE. Even someone withholding information with almost certain knowledge of the commission of a murder?

Senator NUNN. I would hate to be an Internal Revenue Service agent sitting on that information, not so much because of fear of prosecution but for fear of what the consequences would be and fear that I had not done my duty.

Right now in the law the Internal Revenue Service agent would have to kick it upstairs to the top. It would have to work its way through the bureaucracy to the top before a decision could be made. Then a decision would be made.

It depends on whether it is in the return itself or whether it is nonreturn information. But you are right, there is a real paradox there.

Mr. CRANE. Well, it is more than a paradox, it seems to me. It seems to me that when a violation of basic traditional law occurs, the obligations of citizenship would transcend guidelines or something like them handed down by the IRS.

Senator NUNN. I agree with the thrust of that point. I think it is well made, but I believe that the 1976 law basically has the Internal Revenue Service treated different from any other citizen in that respect.

Mr. CRANE. I thank you, Senator.

Chairman RANGEL. Thank you, Mr. Duncan, and thank you, Senator, for sharing the hard work that you put in this area. I have asked staff to work with yours in order to take a look at the examples that you had in your testimony, and certainly that your committee has gone into, to see exactly what is falling between the cracks.

I had some aside conversations with Mr. Crane, and it is just kind of hard for us to believe that evidence of murders can be had and the murderer is running around because the IRS agent can't share it with anyone. Mr. Crane has always come up with examples of what could happen that are exciting.

In any event, we would like to work with you on some of these cases. Rest assured if there is anything that we can do to make the laws more effective as they relate to apprehending criminals, we want to do that.

Senator NUNN. I thank the chairman, and all the members of the committee. I would suggest, if I could, Mr. Chairman, that there be an effort in the next 30 days to have our staff get together because Marty Steinberg, who sits on my right, is going to be departing for the more lucrative practice of law. He knows more about this law and the problems with it than any staffer we have on our subcommittee, and I think probably than anybody on Capitol Hill. So, I would hope that we could contact your staff and have them get together and thrash this out.

Again, I welcome any kind of changes by the committee in a positive direction because there is nothing magic about our direction. We have struggled with it a long time, and I would like to see it simplified. Certainly my expectations are that we can improve the law and, at the same time, protect the privacy of all those concerned.

Chairman RANGEL. We can really start this afternoon to see what schedule can be arranged because we know the problems that exist and the difficulties and sensitivity of this subject matter. We will see what we can work out.

Senator NUNN. I think Senators Roth and Rudman have testimony on this matter. They are supportive of this bill, and I hope their testimony would be placed in the record.

Chairman RANGEL. Without objection.

Congressman Hansen, thank you for waiting so long this morning. The committee welcomes Mr. George Hansen from Idaho.

STATEMENT OF HON. GEORGE HANSEN, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF IDAHO

Mr. HANSEN. Thank you, Mr. Chairman. I guess on this particular controversial issue I am the other half of the odd couple this morning, and I do want to thank you, however, and your subcommittee for granting me this opportunity to express my views on proposed legislation to amend 6103(i) of the Internal Revenue Code.

The goals of these bills—S. 732 by Senator Nunn, S. 1891 by Senator Roth, and H.R. 1502 by Representative Gibbons—may be worthwhile in some respects, but they constitute a very real additional threat to the American taxpayer. One sponsor, upon introducing this legislation in the Senate a week ago, was frank to admit it would repeal even the very limited protections given citizens only 5 years ago in the Tax Reform Act of 1976.

It would appear we are about to experience the third December attempt in a row to slip through the Congress provisions inimical to the rights of taxpayers—provisions aggrandizing to the already bloated power of the IRS and hostile to our American traditions so clearly stated in articles IV and V and other provisions of the Bill of Rights.

In fact, this assault on taxpayer rights is even getting more desperate and more frequent. Earlier this year the provisions of S. 732 were added, as is so often done, at the last minute to H.R. 4242, the Economic Recovery Tax Act of 1981. This unwise piggyback effort was rejected in the conference committee, at least partly because of a strong protest letter I wrote at that time condemning the contents of the amendment and the tactics used to procure its consideration.

It is important to understand what is behind this frantic effort to force these far-reaching measures down the throat of an unwilling Congress and of a people growing more and more suspicious of the willingness of this body to come to grips with the excesses and abuses of the IRS.

The current bogeyman used to induce Congress to further repeal the Bill of Rights is the drug traffic. Much is made of the need to give our law enforcement agencies more authority and power to cope with the wave of organized crime which is engulfing the country. Certainly I share the concern of our citizens and other Members of Congress for the frightening growth of crime and its apparent acceleration in recent years. However, does anyone in this room believe that big time drug dealers include their gains under miscellaneous income in their tax returns? It happened once and made headlines, and even in that one instance, the IRS successfully prevented putting the dealer out of business.

Why then are we even considering further erosion of the rights of citizens in the tax field when we all know that the IRS has virtually withdrawn from the organized crime strike forces. And how do we explain to an aroused public that every time we expand the powers of the IRS they are used against the middle-income taxpayer and not against the criminal? I urge this committee to come to grips with the reality that Congress has used up its store of good will with the people. Clandestine bills which rob them of their rights will no longer be tolerated.

Just how long can the so-called voluntary tax system last if Congress further discourages compliance by scaring off taxpayers who do not want their confidential financial information passed around? In fact, I find the IRS and the Department of Justice already working together to run entire jury venire panels through IRS record control to produce profiles on those potential jurors and even the grand jurors who are the ones who return indictments. Since this same information is denied to defense counsel on the grounds that it would be a felony to release the information, it seems that there is a clear denial of the right to a fair trial for anyone convicted by such a tailored jury.

When I challenged the Justice Department on it, their first answer was that the practice is nearly universal and is authorized by section 6103(H)(5), part of the very section which the proposed legislation would further expand.

In addition, I find the IRS is already circumventing the Tax Reform Act of 1976 without benefit of legislation by getting the local U.S. attorney to issue grand jury summons duces tecum to record holders for direct delivery to the IRS. The reason for the subterfuge, openly stated by Senator Roth in introducing S. 1891, is the fact that taxpayers are becoming aware of their rights to challenge IRS summons and require court hearings to justify Government fishing expeditions.

In another case, an indicted felon was wired for the IRS by the National Security Agency and then sought and obtained work with an organization which the IRS considered to be tax protesters. Upon civil suit, the indicted person admitted that it was done on the promise of the IRS to get the State felony charge dismissed. In the meantime, the organization was under surveillance for over a month.

Mr. Chairman, I would like to make a final point which is not in my statement. I recently asked the General Accounting Office to verify the often quoted claim of the IRS that for every dollar they spend on tax collection $20 is produced. The response is illuminating not only as to that question but as to the reliability of many of the alleged facts on which we ask you to make judgments, particularly hasty judgments, at the end of a session.

GAO's response was as follows: The 20 to 1 figure to which you have referred have been consistently used by IRS in its budget requests and in correspondence and releases concerning its collection activities. Gentlemen, in polite terms the General Accounting Office could not support this very crucial claim of the IRS in its collection ratio, a ratio which has been used as gospel in testimony for years.

Perhaps this is indication that you should look at their statements today with some skepticism, also.

Mr. Chairman, the contention that political abuses rather than law enforcement abuses is the problem is absolutely not valid. Recent court decisions prove this over and over again. Most glaring, the seizure of homes without notice. Can you believe it?

Mr. Chairman, at a time when without official reproach the IRS is collaborating with other Government agencies in illegal electronic surveillance, not against any drug runner or Mafia don, but against the ordinary citizen; when jury tampering is justified in the very name of this section 6103; and when the terms of the 1976 Tax Reform Act are circumvented by unethical collaboration between the IRS and the Department of Justice, always against those average citizens who are the backbone of the country—and rarely if ever against the criminal class—I urge you to reject even the consideration of any more expansion of the power of the IRS.

In fact, Mr. Chairman, the concerns of the American public would be far better served by seriously looking into the misconduct and misuse of the already excessive powers of the IRS and passing my bill, H.R. 4931, the Taxpayer Protection Act. The IRS should be collecting taxes, not scalps.

Thank you.

Chairman RANGEL. Mr. Crane?

Mr. CRANE. I want to thank my colleague for his testimony. You made reference in your testimony to electronic surveillance. Do you have reason to believe that the IRS is involved in illegal use of such techniques?

Mr. Hansen. Mr. Crane, I would like to just wave at you and I can make it available if you want, a document from a court in the U.S. District Court in the District of Colorado, in which this deposition describes exactly that as I described in my testimony; and more than that, that the National Security Agency was involved in helping do the wiring.

Mr. Crane. Mr. Chairman, would it be out of order to include that information in the record?

Chairman Rangel. How much does it weigh?

Mr. Hansen. You might want it for the file rather than the record.

Mr. Crane. At least maybe relevant portions confined to no more than 1,000 words.

Chairman Rangel. Without objection.

[The following was subsequently received:]

In the United States District Court for the District of Colorado

(Civil Action No. 80-C-1734)

John E. Grandbouche, et al, plaintiffs

v.

Pauline Adams, et al, defendants

DEPOSITION OF PAULINE ADAMS, JULY 6, 1981

Appearances: William A. Cohan, Attorney at Law, 1200 Pennsylvania, Suite 6, Denver, Colorado 80203, appearing for the Plaintiffs.

Jefferey A. King, Trial Attorney, Tax Division, United States Department of Justice, Washington, D.C. 20530, appearing for the Defendant, United States of America.

Patrick J. Canty, Attorney at Law, from the law firm of O'Connor & Hannan, 3100 Security Life Building, 1616 Glenarm Place, Denver, Colorado 80202, appearing for the Defendant, Pauline Adams.

Also present: Larry Lovell, Kenneth Batson.

Deposition of Pauline Adams, taken on behalf of the Plaintiffs pursuant to Notice and in accordance with the Federal Rules of Civil Procedure, at Room 154, United States Courthouse, 1929 Stout Street, Denver, Colorado 80294, on Monday July 6, 1981 at 9:45 a.m., before Clydine M. Stevens, Shorthand Reporter and Notary Public within Colorado.

* * * * * * *

By Mr. Cohan:

Q. How would you describe your activities as a person obtaining information that was being turned over to the Internal Revenue Service and particularly Mr. Lovell and Mr. Batson and other people? How would you describe that?

Mr. Canty. I object to the question on the grounds that it can yield no discoverable material. This witness' opinion of how she characterizes her activities——

Mr. Cohan. Fine. I'll withdraw it.

By Mr. Cohan:

Q. Where you told that you were classified as a restricted-source-confidential informant by the Internal Revenue Service?

A. No.

Q. All right. I will, if I may, describe those areas as those of a restricted-source-confidential informant, although that's a bit cumbersome. I think we're—no, I don't know.

A. I don't know what you mean, "restricted."

Q. I don't know what I mean either. I'm just quoting from affidavits from Mr. Lovell and Mr. Mihlbachler in which they agree that you were classified as a restricted-source-confidential informant, that you provided the Internal Revenue Service with documents, and now I have learned from you that you actually were wired for sound, so-to-speak. You had a microphone on your person that was concealed. Could you describe that microphone that was concealed on your person, the set or whatever it was that was attached to you through which conversations in the offices of the National Commodity and Bartering Association were overheard?

A. I don't know anything about it.

Q. What did it look like?

A. Just a—several batteries, that's all.

Q. Some batteries. Did you see—were they in a box?

A. No.

Q. Were they taped on your body?

A. No.

Q. How were they attached to you?

A. Various means.

Q. Depending upon what you were wearing?

A. Yes.

Q. Was the microphone shown to you and designated as this is the microphone?

A. Yes.

Q. Where was the microphone placed?

A. On my shoulder.

Q. On your shoulder. Was it always basically in the same place?

A. Yes.

* * * * * * *

Q. They gave you a regular name like, "My name is Joe Smith"?

A. They would say—they wouldn't say Joe Smith or anything like that.

Q. What would they say?

A. Well, "My name is so and so and such and such."

Q. And these were different people every day?

A. Yes.

Q. Would they be the same people in the evening that took it off as the people in the morning who attached it to you?

A. No, different people.

Q. And you said that you were wired approximately four weeks?

A. Approximately.

Q. So that would have been at least 20 work days?

A. Approximately.

Q. More or less. So there must have been—strike that.

How many people would wire you in the morning, just one, two?

A. One or two or three people; four people sometimes.

Q. So during this period of time in order to get wired, you must have seen on the order of 60 or 80 people; is that correct?

A. No.

Q. It's not? Can you give me a rough idea of how many people you would have seen who would have been wiring you and unwiring you during this period of time?

A. Well, the person that would wire me on Monday morning would be the same person that would wire me on Friday morning.

Q. What about Tuesday or Wednesday?

A. It would have been somebody else.

Q. So some of the people that were involved in the wiring and unwiring would be reappearing several days later. Is that a fair statement?

A. Yes.

Q. Were some of these people the people you saw at the meeting at the hotel that you said on the telephone there were 16 of them, approximately?

Mr. KING. I think she indicated that she didn't say it was 16 on the telephone.

Mr. COHAN. That's what she said today, but she's not sure how many of them there were.

By Mr. COHAN:

Q. You met with some people from the National Security Agency at a hotel in Denver, right?

A. Yes.

Q. Were some of those people involved in wiring you and unwiring you?

A. Yes.

Q. But there were also some involved in the process that you didn't see at that motel or hotel in Denver?

A. Yes.

Q. And you don't know the name of a single one of those people?

A. No.

Q. Did they ever give you any documents?
A. You mean identification?
Q. Yeah. Of any kind. Did you ever see any badges or other types of ID?
A. Yes.
Q. By whom were those people employed according to their identification?
A. Justice Department.
Q. Justice Department, not the Internal Revenue Service?
A. No.
Q. Was Mr. Lovell involved in any of the wirings or unwirings?
A. No.
Q. Mr. Batson?
A. No.

Mr. CRANE. Second, you make reference to jury tampering in your testimony. Do you also have evidence that IRS has been involved in jury tampering?

Mr. HANSEN. Yes, sir, Mr. Crane. I might mention that this is not the only instance of electronic surveillance. This is just a really well-documented one. So as far as the jury tampering is concerned, I won't submit all this for the record, Mr. Chairman, but I have a letter from an attorney in South Dakota accompanied by a document in which he absolutely states that the U.S. attorney was using information procured in the Internal Revenue Service in jury selection and that he was denied the same information on the basis that it would be a violation of section 6103 of the United States Code.

Mr. CRANE. But under existing law it is not a violation to provide that information to the prosecution, is that it?

Mr. HANSEN. My contention is, Mr. Crane, that it is a violation for the prosecutor also, and that the Government is trying to have it both ways, and when they can stack the jury with information that the defendant does not have that this does constitute a real question as to whether it is a fair trial.

Chairman RANGEL. Would the gentleman yield?

Mr. CRANE. Yes, I am happy to.

Chairman RANGEL. Mr. Hansen has requested that the subcommittee look into alleged abuses by the Internal Revenue Service and we have agreed with him that we would hold hearings. I assume that most of the information which he is presenting to us today, he will be testifying about in detail when we hold hearings on that particular point.

Mr. CRANE. Very good. Then I will not now pursue this line of inquiry further. I am concerned about the implications in the testimony of our distinguished colleague from Idaho, and I look forward to those hearings.

Thank you for your testimony.

Mr. HANSEN. Mr. Crane, I might mention that I think there was a lot of colloquy with the previous witness about the fact that the 1976 Reform Act did away with a lot of the possibilities of political abuses of taxpayers. But I might say that there doesn't seem to be anything that has really happened yet to protect the taxpayer against the abuses by the agency personnel themselves. I think that is the one thing that we still need to address.

We may have taken away the Watergate syndrome but we haven't taken away the bureaucratic syndrome.

Mr. CRANE. May I be excused for one more question? Under existing law, the IRS, it states, is authorized but not required to disclose return information that may constitute evidence of a violation of Federal criminal laws. Whereas in H.R. 1502 and Senate bill 1891, the bill would require the disclosure of such information?

I get the impression from your testimony that while the IRS is authorized to disclose such information, the insistence that they be required to do so is not necessary, because even under existing law because they are cooperating and are disclosing information to other agencies; is that correct?

Mr. HANSEN. As I understand on a case-by-case basis that they can do it through proper court order but not on an indiscriminate or wholesale basis such as I have cited here.

Mr. CRANE. I see, thank you.

Chairman RANGEL. Mr. Jenkins?

Mr. JENKINS. Thank you, Mr. Chairmman, I just have one question.

When you are talking about jury tampering there might be a question as to the definition of the term. I assume what you are talking about is a case in which the U.S. attorney has requested the Internal Revenue Service to give him information on an entire panel of jurors as to whether they have had an audit or difficulties with Internal Revenue that might indicate some bias on the part of the prospective juror, that type of information?

Mr. HANSEN. That is correct, but doing it with the whole panel, not select instances through court processes as is spelled out by the law now.

Mr. JENKINS. Of course, this has been done for a long time, I am sure, by U.S. attorneys. Certain information is turned over to them. Are you saying that under the existing law that is authorized?

Mr. HANSEN. As I understand existing law, Mr. Jenkins, all they are entitled to are yes or no answers, and it is very, very restricted and it is also on a very select basis. It is not on a wholesale basis. Right now we have reason to believe that the IRS is disclosing much more information than they should on a much broader basis than they should extralegally.

Mr. JENKINS. And your position is that the Internal Revenue Service should be precluded from giving any information regarding a prospective juror to the prosecutor; is that right?

Mr. HANSEN. Well, Mr. Jenkins, I think that the whole concept of the Internal Revenue Service and tax compliance and we all know we have to have taxes to make this government run, so this is not the idea of being opposed to taxes. It is how do you make the system work. And they talk about the big underground economy and so forth, but if you are chasing people out of the system because they are afraid to get involved with the system, then I think it is extremely dangerous. So I think that the hatches should be battened down absolutely as tightly as possible. Even on the assumption that maybe you don't even have such a thing as an Internal Revenue Service, that you have a different kind of tax collection service.

In other words, I don't think the Department of Justice or anyone else should depend for its own prosperity, so to speak, or ride piggyback on the Internal Revenue Service.

Mr. Jenkins. I think you are right that U.S. attorneys have obtained information on prospective jurors and probably that is provided by IRS. I don't know if they still do this. I know that they used to do this prior to 1976.

Mr. Hansen. They still do.

Mr. Jenkins. It is your contention that this should not be allowed; is that right?

Mr. Hansen. That is correct. And this letter, I might mention, is dated September 23, 1981, with the complaint so this is very recent, this happening.

Mr. Jenkins. Thank you.

Chairman Rangel. Mr. Moore?

Mr. Moore. No questions.

Chairman Rangel. Mr. Duncan?

Mr. Duncan. I have no questions.

Chairman Rangel. Thank you very much, Mr. Hansen. We look forward to the additional information that you have for the committee.

Mr. Hansen. Thank you, Mr. Chairman.

Chairman Rangel. The committee is honored to have three former commissioners of the Internal Revenue Service, whose reputations have been enhanced since they retired. We have Mr. Sheldon Cohen, who served under the Johnson administration; Mr. Donald Alexander, who served under former President Nixon; and Mr. Jerome Kurtz, who served under the Carter administration.

We sincerely thank you for taking time out to share your views on this very delicate subject matter and we are very interested in learning what you think of the legislation that is before the committee.

The full committee and the subcommittee welcomes you.

Mr. Cohen?

STATEMENT OF SHELDON COHEN, FORMER COMMISSIONER OF INTERNAL REVENUE

Mr. Cohen. Well, I guess I am senior in terms of service, sir, so I will go first. Thank you, Chairman Rangel and members of the committee. I appreciate your inviting me here this morning. I was made aware of this hearing only a few days ago, so I apologize for not having a written statement.

I appeared before the House Rules Committee last week to discuss with them the concept of tax expenditures. At that time my discussion did not go off on the ideology of tax expenditures, whether there are such things or whether there are not, it was on the administrative burdens that the Congress constantly places on the Internal Revenue Service. In the IRS, we have an agency which is considered one of the better, probably the best administrative agency of the U.S. Government. It is being pushed to the brink of inefficiency by one more job, one more job and one more job. And if you will forgive me, I will refer you to the testimony before the Rules Committee. I have a few copies here. Perhaps a member of your staff could bring them up to you.

For example, in the Labor Department area, job subsidies and pension qualifications are handled by the IRS. The Energy Department normally would consider energy credits, depletion allowances, other encouragements for exploration but that, too, is an IRS function. The Agriculture Department should handle farm subsidies.

In the Commerce Department area we have DISC, we have foreign sales operations we have IDB's. In Housing we have housing subsidies and we also use IDB's. We have tax exemption provided for educational institutions which is what the Education Department should be doing.

In the Transportation Department we have all sorts of subsidies including subsidies for airlines, airports, whatever. Then, in the Justice Department we have law enforcement and the question is where ought general law enforcement occur in our Government. Generally, we have answered that general law enforcement ought to occur in the States and Federal law enforcement ought to occur in the Justice Department.

That is not to say that the IRS does not have a law enforcement function. I am the last one to say that it should not. I am the person who authorized the first 26 man-years to be used in an experiment with the organized crime effort. But should the IRS use 20 percent or 25 percent of its criminal law enforcement effort to perform a job outside its regular function? I venture to say no. At the height of its activities, the service was using something on the order of 20 to 25 percent of its criminal law enforcement personnel on strike force or related matters.

The IRS has a broad, difficult job. It is a difficult job to collect taxes. The service is given a variety of powers that we don't give to other agencies. The FBI does not have the right to go into a taxpayer's records without court order. The IRS does. The FBI and other law enforcement agencies do not have other powers that the IRS has been granted.

The reason for the grant of these powers is that the U.S. Government cannot exist without a tax power. Therefore, we ought to be very chary of broadening the activities of the IRS to include activities of other agencies, lest those powers that we have granted for limited purposes be used for much broader purposes. And that is exactly what those prosecutors are after.

They are after short circuits to the usual procedural rights and rules. It happened in my day. I am sure it happened in these gentlemen's day. It is happening today and it will happened in the future.

I had the privilege of being on a committee of the Administrative Conference which studied the administration of the Internal Revenue Service in the period before 1975. There is a report of that group. Senate Document 94-266, which is entitled "Administrative Procedures of the Internal Revenue Service," dated October 1975, report to the Administrative Conference of the United States. In that report, which is about 1,200 pages long, there is a chapter dealing with this important problem of taxation privacy. It is chapter 6, and I would hope that your staff and some of you will have the opportunity to read the conclusions portion. That material summarizes the complete history of the disclosure of tax returns.

We have swung the pendulum back over our history, more disclosure, less disclosure, and rather restricted disclosure. Our citizens seem to have confidence in a very restricted disclosure. I would recommend to you that you maintain that restricted disclosure.

There are some technical provisions which the American Bar Association's tax section are going to discuss with you later. After a careful study they will recommend modification of some provisions of this bill in terms of the degree of the penalty. I believe the tax section has taken a reasoned approach. But prosecutors are like everyone else. They want access to information and they want it easy. The fact is that they can obtain most information in an ex parte proceeding at which they merely need to say that they need tax information for the investigation of Mr. X or Mr. Y and that the financial records will aid them in determining certain things. They also have to say that they have reason to believe he has committed some sort of a crime. However many prosecutors haven't bothered to apply. They haven't bothered because it requires a little paperwork.

A revenue agent can't go to the file under current administrative procedures of the Revenue Service without creating a paper record which should have need for such records. A tax return has my innermost financial secrets and should not be shared with other departments except in a showing of urgent need within the rules proscribed by law.

There has to be a careful, controlled access, and I believe that the 1976 act, in general, struck a careful balance.

From the day that the 1976 statute was passed, there have been attempts at each session to defer its operation. In fact, the 1976 act had not even come into effect and there was a hearing before the Ways and Means Committee where several members of the Justice Department appeared in an attempt to suspend the administration of these privacy provisions of the Internal Revenue Code before they were effective. They had not started operating. The Justice Department had no reason to be concerned. They hadn't been deprived of anything but they were concerned. If I were a prosecutor I would probably be here saying I want easier access. A prosecutor's job is to prosecute. Congress job is to impose those balanced controls that make the internal revenue system work. This is the essential thing which has not been discussed this morning.

We have a magnificent tax system. It is an extremely valuable asset of this country that our taxpayers pay and report most of their income voluntarily. Not all of it but most of it. We are falling woefully behind in the enforcement of our tax laws. We cannot afford the diversion of personnel in cops and robbers exercises even though those may be good exercises for our society. They are good exercises for another agency created in our society.

The Revenue Service has too much to do to divert its efforts to these, even though they are serious efforts. Recently the GAO has reported that the organized crime efforts have not really borne fruit. There ought to be a reexamination of that whole effort.

You cannot blame failure of law enforcement on the Internal Revenue Service. Surely the Congress and the Justice Department, and indeed the whole Government, ought to examine the way we operate to make sure that the Justice Department has adequate tools. But access to tax returns is not going to be a panacea. What will happen is that revenue agents and special agents of the Internal Revenue Service are like everybody else. They like to be where the action is. If you make this glamorous, they are going to diffuse their efforts into pure law enforcement more and more and they will expend less and less efforts on the collecting of taxes. I think that tax collection is the job of the Internal Revenue Service, Mr. Chairman.

Chairman RANGEL. Thank you.

[Mr. Cohen submitted the following:]

TESTIMONY OF SHELDON S. COHEN ON TAX EXPENDITURES

My concern today is not with the ideology of tax expenditure—or with those who contend that since the government has no right to an individual's property, there is no such thing as a tax expenditure.

In either case, respect for our tax laws requires that they be administered fairly and equitably. The burden of this responsibility falls on the Internal Revenue Service, and by and large it fulfills its role well. That is both a blessing and a curse: a blessing because a strong and fair tax system, effectively administered, is necessary to a democratic society; a curse, that because of this very efficiency more and more jobs are asked of it.

Tax administration, like most other things, is subject to the law of diminishing returns. The more elaborate the tax system—and the more objectives attempted by the use of the tax law and the more the administrative responsibilities we expect of the IRS, the less efficient our system will be.

It does not take much imagination to see the IRS saddled with most of the jobs of the: Labor Department (job subsidies, pension qualification); Energy Department (energy credits, depletion deduction, other encouragements to exploration); Agriculture Department (farm subsidies); Commerce Department (DISC, foreign subs & sales, IDB's); HUD (housing subsidies); Education (tax exemptions for education); Transportation (airport subsidies); Justice (law enforcement activities); etc., etc.

This picture is not as silly as it may sound. If we were to continue the present proliferation of tax incentives or dis-incentives much longer, we could abolish the other departments of government and let the IRS do it all. I suggest to you and believe that most members of Congress would agree that this is not sound policy.

My concern is that we have taken a fine administrative agency and are pushing it toward inferior performance. We expect too much. A revenue agent is not a social worker, teacher, housing expert, oil and gas engineer, policeman, or all of the other things we are calling on him to be.

The Congress and each new administration preaches that we should simplify our tax laws. This is an important goal, but it can never be achieved so long as you, the Congress, insist on attempting to cure every economic and social disease with a tax provision. The quick fix will create bad law—and inadvertently will destroy a good administrative system.

We must reexamine this drift before it is too late. I believe we still have time, but this Committee and the leaders of Congress must act to stop the use of our tax laws for such a multiplicity of purposes.

Chairman RANGEL. Former Commissioner Donald Alexander?

STATEMENT OF DONALD C. ALEXANDER, FORMER COMMISSIONER OF INTERNAL REVENUE

Mr. ALEXANDER. Thank you, Mr. Chairman. I have a written statement, and with the permission of the committee I would like to file it but not read it.

Chairman RANGEL. Without objection.

Mr. ALEXANDER. Mr. Chairman, I want to associate myself with what my predecessor, Sheldon Cohen, said this morning. I do find, however, some things that could stand some improvement in the amendments made in 1976, and I recall very well being Commissioner at the time and being here at the Hill. My effort at that time was to try to assist the Congress in arriving at a sound balance between the obligation of the Internal Revenue Service to be a part of our National Government and to supply information to others under carefully restricted circumstances and the obligation of the Internal Revenue Service to do what former Commissioner Cohen said, to administer and enforce the tax laws and to protect the privacy of the vast supply of information given to it.

There were charges, as you recall very well, Mr. Chairman, in the middle 1970's and early 1970's about IRS being a lending library for other agencies, departments and people in the Government. And to some extent those charges were correct.

There was concern, and correctly so, on the part of IRS leadership in those times about not only political abuse of the IRS and its information and its people but misuse of the IRS to make it a general purpose law enforcement agency at the expense of the tax system. At the expense not only of the revenues but at the expense of the taxpayers who are willing to shoulder their burdens when others, thanks to insufficient resources of the IRS then and now, were not called on to shoulder theirs.

Now, in the proposals that are under consideration today there are, I think, needed improvements to what was accomplished in 1976. The procedure of obtaining a court order to require tax information for use in a nontax criminal investigation could be simplified, speeded up and made more workable, I would think, without any great deprivation to taxpayers' rights of privacy or to the job of the Internal Revenue Service. But there are some very serious problems in the legislation before you, and I attempt to summarize these in my statement.

One is the substitution of a requirement that the IRS turn over to other agencies information that it may have that is received from other than the taxpayers' voluntary submission that may constitute evidence of a violation of Federal criminal law.

In the first place, this requirement might well be construed for the reasons that former Commissioner Cohen described, and others, as a directive to the IRS and its criminal investigators, that their job is to seek out information that might show a violation of another law rather than engage in the enforcement of the tax laws.

Second, we have a problem of the inadvertent violation of law. A catch 22 is really created here as opposed to the hypothetical catch 22 that was described this morning without reference to the provision in the law which currently authorizes the Internal Revenue Service to turn over information which may constitute evidence of a violation of criminal law. Here we would have a real catch 22 because there is a duty on the Internal Revenue Service to turn over information which may constitute evidence of the violation of a non-tax criminal law, yet how is the Internal Revenue Service to know that the evidence and material in its possession which it has acquired in an investigation or an audit constitutes such evidence?

Second, returning to a point that former Commissioner Cohen described, we find a provision that appears to be remarkably unnecessary to the goals sought by this legislation. This is, I believe, in both the administration's bill and the bill that Senator Nunn and others are proposing, "no portion of this section shall be interpreted to preclude or prevent the Internal Revenue Service from assisting the Department of Justice or other agencies in the nontax investigations of criminal matters which may involve income tax violations," nor can it preclude or prevent the IRS from investigating or gathering relevant information concerning persons engaged in criminal activities "which may involve income tax violations."

This will be construed in the real world in which we live, if that provision becomes law, as an open invitation to the IRS to become a law enforcer not of last resort but of first resort, to take over the job that the DEA appears to be still unable to do and to take over the job of collecting information which might have some tax relevance, but which is collected for the purpose of trying to find out whether a particular person has committed a non-tax crime.

The IRS has no business engaging in this broad scale, general purpose, criminal enforcement effort even if it could legally do so. And in my statement I mentioned the legal restriction on the IRS summons power set forth in the *La Salle National Bank* case.

Second, the IRS doesn't have the personnel, the resources in people, in money or in powers to enforce the tax laws as effectively as all of us in this room would like. If its powers must be further diverted and its people must be used for non-tax purposes, then who is going to make our tax system work?

[The prepared statement follows:]

STATEMENT OF DONALD C. ALEXANDER

My name is Donald C. Alexander and I am a partner in the Washington office of Morgan, Lewis & Bockius. I am appearing, solely in my personal capacity, at the invitation of the Subcommittee to discuss various proposals to amend Section 6103 of the Internal Revenue Code. The proposed amendments would increase access of the Department of Justice and others to Internal Revenue Service information.

In 1976 Congress took important steps to protect the records of taxpayers, whose voluntary participation in our revenue system is crucial. The Tax Reform Act of 1976 provided a system to safeguard the privacy of taxpayer records, except in those clearly defined cases where disclosure of tax returns, or underlying information, is vital. IRC Section 6103, as adopted by Congress after extensive hearings and debate, represents a careful balance between the competing interests of government agencies that need access to tax information in order to carry out their functions, and the legitimate expectations of taxpayers that their tax matters will be kept private. Before removing such protections, Congress should carefully weigh the anticipated benefits of the changes against the potential determinents to our tax system.

Today the job of the IRS is to administer and enforce the federal revenue laws. No other agency has this responsibility. IRS lacks the resources to do its own job and also serve as the Government's general purpose law enforcemnt agency In the past, the IRS filled a void in the law enforcement area by supplying its personnel and information to others. In filling that void, thinly stretched IRS personnel were stretched even further, making it very difficult for the Service to fulfill its tax responsibilities. In addition, the freedom with which IRS handed over its information led to serious problems, abuses that were acknowledged by Congress and corrected by the 1976 Tax Act.

Today, our law enforcement agencies have been expanded and strengthened. The Drug Enforcement Administration is charged specifically with enforcement of drug laws, and the FBI also has responsibilities and duties in the control of drug traffic. To the extent that concerns about drug trafficking are the motivating force behind the proposals under consideration today, we should make sure that these agencies with first-line responsiblity for law enforcement have sufficient resources to do their jobs effectively. In view of the Administration's concern about our national drug problem, I am puzzled by the Administration's effort to reduce the DEA's appropriation.

Tax returns and tax agents should not be used as a substitute for non-use or misuse of existing law enforcement tools. This is not to say that the IRS should play no role. It should, and it does, enforce the tax laws against drug traffickers who evade taxes, and many do. While drug trafficking appears to have been the impetus for these proposals, the proposed amendments apply to violations or even merely suspected violations of any federal law and would be applicable to all corporate taxpayers of two or more shareholders and all partnerships and associations with two or more members.

Proposed amendments would require the IRS to disclose to federal agencies any third-party information and the underlying records of larger corporations, partnerships and associations containing evidence of nontax violations of federal criminal laws. These same proposals would provide that the Department of Justice would have free access to any return or nonreturn information when the IRS makes a criminal tax referral. Both these proposals are troublesome. IRS now has the right to report criminal activities, and the better course is to improve administration, not to impose a duty which might well be interpreted to force IRS into a role as a general law enforcement agency, the first-line gatherer of evidence of violations of laws enforced by other federal agencies. The proposals also raise the potential of using referrals to transfer sensitive taxpayer information to other federal agencies.

Not only taxpayer privacy would be affected. The proposals would present IRS officials with the following conundrum. IRS agents are trained to discover and investigate violations of our tax laws, not other laws. Yet the proposed amendment would require them to report evidence of any violation of any Federal criminal law. This puts these same agents in the unenviable position of being required to report violations which they may not even recognize. Criminal violations of the Federal antitrust laws are a good example of this. The IRS may, therefore, find itself in violation of the law requiring it to hand over evidence of nontax crimes.

Certain proposals before this Subcommittee are clearly designed to cause the IRS to play a more central and active role in general law enforcement. In particular, the Administration proposal, like Senator Nunn's, states that nothing in Section 6103 is meant to preclude or prevent IRS "from assisting the Department of Justice or any other Federal agency in joint tax and nontax investigations of criminal matters" which may involve income tax violations or "from investigating or gathering relevant information concerning persons engaged in criminal activities which may involve" income tax violations. This appears to authorize the use of IRS personnel and powers far beyond the scope of tax-related activities, and could be construed to make the IRS an investigative arm of the Justice Department. IRS participation in the overall enforcement of our laws is desirable but the proposed language has the potenial to involve the Service in activities having little, if any, relationship to the enforcement of tax laws. The IRS should not expend its limited resources in this matter, even if it could legally do so. In limiting IRS's use of its summons power, the Supreme Court stated in *United States* v. *LaSalle National Bank*, 437 U.S. 298, 317 (1978) that "the good-faith standard will not permit the IRS to become an information-gathering agency for other departments, including the Department of Justice, regardless of the status of criminal cases."

Procedures under current law to obtain court-ordered disclosure of taxpayer information have been criticized as being so cumbersome and time-consuming that the Department of Justice finds it very difficult to obtain necessary information. While I am not aware that any Justice request for a court order has ever been denied, I support proposed amendments to streamline an unwieldy system. Proposals permitting U.S. Magistrates to issue such orders and permitting Justice Department attorneys in the field and U.S. Attorneys to apply for such orders make sense.

Proposed modifications in the standards for obtaining a court order will, I believe, also make the system more workable. Disclosure of return information to Department of Justice officials in a nontax criminal investigation, pursuant to an ex parte court order, should be permissible if the requesting federal prosecutor can demonstrate reasonable cause that a specific federal crime has occurred and that the tax return contains relevant information. To the extent that the court order procedure itself is retained for all taxpayers, corporate or individual, a reduction in the required standard of proof from that under current law should not jeopardize taxpayer protection.

In conclusion, I would like to reiterate that in 1976 Congress adopted a workable system to deal with the competing interests of those seeking disclosure of tax returns and return information and the taxpayers' rights of privacy. This system can be improved and certain of the proposed changes are desirable. However, taxpayer compliance and tax administration will suffer if the basic balance is altered to make IRS a lending library to law enforcement agencies or if IRS is required to expend its limited resources in the enforcment of nontax laws.

Chairman RANGEL. Thank you.

Former Commissioner Jerome Kurtz.

STATEMENT OF JEROME KURTZ, FORMER COMMISSIONER OF INTERNAL REVENUE

Mr. KURTZ. Thank you, Mr. Chairman.

I find myself in virtually complete agreement with what has been said before. Let me say I have a written statement I would like to submit for the record, if I may, and I will summarize it in my testimony.

Chairman RANGEL. Without objection.

Mr. KURTZ. The bills before the committee would make a number of changes to 6103, a number of which I think properly can be classified as technical, although some have their own problems. But I would like to limit my testimony just to what I consider the most critical changes which are proposed in this legislation.

Basically, under the present statutory scheme of section 6103, information which is received by the taxpayer, either in his returns or during the course of an examination can be disclosed only pursuant to a court order requested by a senior official of a Federal law enforcement agency. The agency must show that it already has a proceeding or an investigation underway and that the tax information is likely to be evidence.

In general, a taxpayer's information in the hands of the Service is protected in much the same way that it would be protected if it remained in the taxpayer's hands, in which case a search warrant would be required. The requirements of 6103 in this regard, while they are not identical, are essentially similar to the requirements for obtaining a search warrant.

The protection that is afforded information that the Internal Revenue secures not from a taxpayer but from a third party has a lesser degree of protection because the taxpayer doesn't have the same claim to confidentiality of information which is not in his possession and which he didn't turn over to the Service.

S. 732 would change that basic statutory scheme in the case of information obtained from entities such as corporations, partnerships, associations, labor unions, et cetera, that have two or more owners, partners, shareholders or members. Tax information obtained in those cases during the course of an audit could be turned over to a Federal law enforcement agency upon a simple written request.

Moreover, and perhaps even more importantly, the Internal Revenue Service would be required to forward to Federal law enforcement authorities any information of a nontax crime that was uncovered in the course of an examination.

For all taxpayers, including individuals, S. 732 would require that when the Internal Revenue Service makes a recommendation to the Justice Department for prosecution of a tax crime it turn over everything that is in the file whether or not relevant to the tax crime, and the Department of Justice would then be free to use such nonrelevant information to develop a nontax crime if it were indicated.

S. 732 would also permit Federal prosecutors to obtain a court order to redisclose information dislcosed to it to State and local law enforcement agencies.

The problems that these proposed revisions raise are primarily the following:

They would seriously interfere with the Service's primary responsibility to enforce the Internal Revenue Code and to collect taxes. In examining a taxpayer it is important, if it is to be done efficiently and effectively, that the revenue agent have access to the taxpayer's books, records, files, anything that may bear on the tax liability. If these provisions are in effect, I am afraid as to those entities affected—corporations, et cetera—that an examination would become a game of hide and seek. Taxpayers naturally and justifiably would be reluctant to turn over files, books, and records if they realized that any evidence of any nontax crime that happened to be lurking in those files would immediately find its way through the internal revenue agent to the Department of Justice.

The Service has run into problems in the past in obtaining certain information from taxpayers. Major corporations have tried to withhold certain information, and there has been some recent litigation concerning the Service's right to obtain such information. By and large, courts have been sympathetic to the Service's position.

I am concerned that if information once in the hands of the Service had to go to the Department of Justice such information would not as readily be disclosed by taxpayers. There would be more resistance and I am afraid courts would be much more sympathetic to a taxpayer's claim for withholding information from the Service.

It seems completely clear to me that these provisions would divert some agents' attention from their primary job of verifying a taxpayer's income to digging around for tidbits of information in the taxpayer's files to refer to the Department of Justice. Again, this would be a dissipation of very scarce resources of the Internal Revenue Service with what I am virtually certain would be minimal law enforcement gains.

The same can be said of the provisions which would require all information in a criminal tax file to go to the Department of Justice. Such a rule obviously would encourage the investigators working on the tax case to fill the file with information which may indicate nontax crimes on the assumption that it would go over at the time of the referral and the Department of Justice could use it.

During fiscal year 1980, the Internal Revenue Service examined 140,000 corporate income tax returns. Over 20,000 partnership returns and about 24,000 returns of exempt organizations. The changes proposed by this bill in effect say, here is a license to do over 200,000 door-to-door searches—see what you can find. One must keep in mind that the 200,000 examinations I refer to weren't done because there was any suspicion that the taxpayers involved had been involved in any crime. By and large they are a function of routine civil tax administration and are selected solely on that basis. To turn every routine tax examination into a general fishing expedition for evidence of criminal misconduct I believe would be a vast misuse of Government power and of Government resources.

A potential for mischief is inherent in S. 732 and other bills similar to it which is very troublesome. It seems to me it is but a short step from requiring the Internal Revenue Service to turn over to the Department of Justice any criminal evidence that comes cross in the course of a routine audit to the next step of the Department of Justice requesting the Internal Revenue Service to do a civil examination to see what evidence of nontax criminal activity it might come across in the course of that examination.

These are very serious problems. The tax system can only work if taxpayers acquiesce in it and cooperate. In my view, that cooperation requires that the Service keep to the business of enforcing the tax law and not become a stalking horse for every prosecutorial agency in the Federal Government.

I might say a word about the provision for redisclosure of tax information to State and local law enforcement agencies. There are over 19,000 such agencies in the United States, half of them with fewer than 10 employees. It would appear impossible for anyone to be able to insure the confidentiality and proper use of such information once it were required to be turned over to such a vast array of law enforcement agencies.

I believe there is very little wrong with 6103 as it now exists. That is not to say that it has worked perfectly by any means. There are technical changes which should be made. There are administrative changes which have been made and additional ones which should be made.

We have heard testimony this morning that U.S. attorneys do not effectively obtain information pursuant to court orders under 6103. First, I think it is worth noting that a request for a court order to get tax information under section 6103 has never been turned down to my knowledge.

Second, the provision is used extensively by some U.S. attorneys. The last time I got information from the Department of Justice, which was, at this point, 1½ or 2 years ago, there were a substantial number of U.S. attorneys—my recollection is almost half—who had never applied for a court order under 6103.

While the use of section 6103 court orders are not great, there are several hundred instances, all successful, which tend to be concentrated in certain U.S. attorneys who understand the provision and know how to use it, which leads me to the conclusion that an educational effort by the Department of Justice concerning the existing rules would not be out of order.

Let me conclude by saying that the Internal Revenue Service has an important role in the fight against organized crime and drug trafficking. That role is to prosecute those who evade their income tax liabilities including organized crime figures and drug traffickers who, as we know, are particularly prone not to live up to their tax obligations.

But the IRS can fulfill that role within the context of evenhanded tax administration. It should not be required to act as an arm of the Department of Justice or of the Drug Enforcement Agency.

Thank you, Mr. Chairman.

[The prepared statement follows:]

STATEMENT OF JEROME KURTZ

Mr. Chairman and Members of the Committee, I am pleased to respond to your invitation to share with you my views on proposed amendments to Section 6103 of the Internal Revenue Code. My concern about these matters results from my service as Commissioner of Internal Revenue from early 1977 until the fall of 1980. I am now a practicing attorney in Washington, D.C., and appear in my individual capacity.

Section 6103 of the Internal Revenue Code protects the confidentiality of tax information received or collected by the Internal Revenue Service. It provides that such information may not be disclosed by the Service to anyone, for any purpose, except as specifically permitted under that section. The legislation before you would expand those exceptions primarily as they relate to the disclosure to law enforcement agencies of information concerning non-tax crimes.

Under existing Section 6103, disclosure of such information may be made only under the following circumstances:

1. If the information was filed with or furnished to the Service by or on behalf of the taxpayer it may be disclosed only pursuant to an ex parte order issued by a Federal district court judge on application by the head of the Agency seeking the information, or, in the case of the Department of Justice, the Attorney General, Deputy Attorney General or an Assistant Attorney General, upon a determination that, (1) there is reasonable cause to believe a specific criminal act has been committed, (2) there is reason to believe the information is probative evidence of a matter in issue related to the crime, and (3) either that the information cannot reasonably be otained from another source or that it is the most probative evidence.

2. If the information was obtained from a third party rather than from the taxpayer, it may be disclosed in reponse to a written request from the head of the Federal agency or from the Justice Department officials named above specifying the taxpayer's name and address, the taxable periods involved, the statutory authority for the investigation or proceeding and the specific reasons why the disclosure may be material to the investigation or proceeding.

3. The Internal Revenue Service may, on its own initiative, disclose in writing, to the head of the appropriate Federal agency, evidence of a criminal violation obtained from third parties.

Thus, under the present statutory scheme, information received from the taxpayer, either in his or her return on in the course of an examination may be disclosed only pursuant to a court order requested by a senior official of a Federal law enforcement agency which requires the agency to show that it already has a proceeding or investigation in progress and that the information is likely to be evidence. In general, a taxpayer's information in the hands of the Internal Revenue Service is protected in much the same way as it would be protected if it remained in the taxpayer's hands. In that case a search warrant would generally be required for a Federal law enforcement agency to gain access to such information. The requirements for the ex parte order under Section 6103 are similar to those required for a search warrant.

The protection is of a much lesser order where the information is obtained from third parties because the taxpayer does not have the same claim to confidentiality of information not in his possession.

The bills before the Committee would make a number of changes to Section 6103. Many of the changes may properly be characterized as technical—designed to make the existing scheme of protection and disclosure work somewhat better, although some present their own problems. I would be pleased to discuss these with the Committee or its staff and will limit my comments here to what I consider the issues of major importance.

S. 732 would change the basic protection afforded tax information obtained from entities such as corporations, partnerships, associations or unions, with more than two owners, shareholders, partners or members. Tax information obtained from such entities during the course of a tax examination could be obtained by Federal law enforcement agencies pursuant to a simple written request rather than by ex parte court order as now required. Moreover, and even more importantly, the Internal Revenue Service would be required to forward to Federal law enforcement authorities any evidence of a non-tax crime it uncovered in the course of a routine tax examination of such entities.

For all taxpayers, including individuals, S. 732 would require that when the Internal Revenue Service makes a recommendation to the Justice Department for prosecution of a tax crime, all information collected by the Service, whether or not relevant to the criminal tax referral, be sent to the Department of Justice, which would then be free to use such information to develop non-tax criminal cases.

S. 732 would also permit Federal prosecutors to obtain a court order to redisclose tax information received from the Internal Revenue Service to State and local law enforcement agencies to be used by them in connection with the prosecution of State non-tax felonies.

These proposed amendments to Section 6103 would affect the policy reflected in Section 6103 in a fundamental way. The result of these changes would be to diminish the confidentiality of tax information which taxpayers have a right to expect, seriously interfere with efficient tax administration, distort the mission of the Internal Revenue Service and open the potential for great mischief.

The basic premise of the present system of safeguards is that tax information furnished to the Internal Revenue Service by the taxpayer either in his return or in the course of an examination may not be used to generate a non-tax criminal investigation. Such information is available to Federal law enforcement agencies only if they have an independent investigation or proceeding already underway; that is, if the non-tax crime is the subject of an existing inquiry developed from sources other than tax information. There are compelling reasons to continue the existing system.

First, the existing system does not, and the revisions would, force the affected taxpayers to cheat on their taxes or withhold records from the Service to avoid implicating themselves in a non-tax crime.

Requiring the Internal Revenue Service on its own initiative to disclose to Federal law enforcement authorities information it comes across during the course of an examination would seriously interfere with the Service's ability to carry out its function of verifying the taxable income of such entities. For example, in examining a taxpayer the Internal Revenue Service must have free and easy access to virtually all of the information that the taxpayer maintains if the examination is to proceed efficiently and not as a game of hide-and-seek. While some taxpayers, particularly some major corporations, have resisted claims of the Internal Revenue Service for access to certain information, the courts have generally supported the Service. If every document, record or file given to the Service carried with it the potential of informing a Federal law enforcement authority of a possible non-tax criminal violation, taxpayers would be much less cooperative in disclosing such information and the courts would probably be somewhat more supportive of the corporations' reluctance, with the result that the efficiency of the Service in carrying out its primary mission would be seriously diminished.

Moreover, I am afraid that the proposed amendments would inevitably divert some agents' attention from their main function of tax administration to digging around in taxpayers' records looking for interesting tidbits of information to refer to the Department of Justice—again, a dissipation of very scarce resources with what I am virtually certain would be minimal law enforcement gains.

The same can be said of the provision of S. 732 which would require the service to forward to the Department of Justice all information in a taxpayer's file when a criminal tax referral is made. This would encourage Service personnel to collect information, irrelevant to the tax investigation but bearing on a possible non-tax crime, with a view to forwarding it to the Department of Justice.

During the fiscal year 1980, the Internal Revenue Service examined 140,000 corporate income tax returns, over 20,000 partnership returns and about 24,000 returns of exempt organizations. The changes proposed by this bill are in a way equivalent to saying to a Federal agency, "Here is a license to do 200,000 door-to-door searches—see what you can find." One must keep in mind that tax returns are selected for examination not because there is any reason to believe that the taxpayer has engaged in any misconduct, but simply as a part of tax administration. To turn routine tax examinations into general fishing expeditions for evidence of criminal misconduct would be a vast misuse of government power and resources.

The potential for mischief which inheres in these provisions of S. 732 lies in the temptation they present to the Department of Justice to try to direct Internal Revenue Service examinations. It is but a short step from requiring the Internal Revenue Service to turn over to the Department of Justice any criminal evidence it comes across in the course of an audit, to the Department of Justice requesting the Internal Revenue Service to do an audit to see what evidence it might come across. The present provisions of Section 6103 effectively prevent this pressure because such information cannot be turned over unless the Justice Department already has an investigation underway.

A similar risk arises from the provision requiring the entire file to be turned over in a criminal tax referral. The Internal Revenue Service might be encouraged by the Department of Justice to develop evidence of non-tax criminal activity irrevelent to the tax investigation because if there is a tax referral the Justice Department knows it will get such information. The provision also provides a temptation to the Justice Department to pressure the Service to make criminal tax referrals because of the non-tax information contained in the files in situations where the Service, as a matter of tax administration, might not be inclined to do so.

These are serious problems. Our tax system can only work with the general acquiesence of taxpayers. That acquiesence requires confidence that the Internal Revenue Service is in the business of enforcing the tax law and is not a stalking horse for every prosecutorial agency in the government.

The provision of S. 732 which would permit tax information of a more than two-person entity to be obtained by a Federal law enforcement agency by simple written request, rather than court order, would obviously diminish the protection afforded such information. The impartial determination of the necessity for law enforcement agency to have the information would be eliminated. Even more troublesome than the elimination of the court order requirement is the fact that under S. 732 such information may be requested not only by the Attorney General, the Deputy Attorney General, or an Assistant Attorney General as is now the requirement for obtaining third party information, but by any designee of the Attorney General. This provision would permit these requests for a taxpayer's information to be made by a Federal investigator in the field. By permitting delegation to this level, a substantial amount of accountability and responsibility is eliminated and we might well expect such requests to proliferate substantially. Law enforcement personnel directly engaged in a criminal investigation may understandably be less sensitive to privacy issues and tax administration considerations than high level supervisory officials.

The Administration's proposal contained in S. 1891 varies from S.732 in several respects. It would require the Internal Revenue Service to furnish information concerning the non-tax crimes of corporations and other entities, only if it were first determined that the entity was "formed, or is being operated or maintained for the criminal purpose." While this is an attempt to narrow those cases where information must be forwarded, it is not at all clear how the determination that the entity was formed, operated or maintained for criminal purposes is to be made, what standards are to be applied, who is to make the determination and, in fact, whether the taxpayer is entitled to any review of such determination once made. If evidence of a crime is uncovered, does this provision mean that the entity is maintained for a criminal purpose. If so, the provision would seem to accomplish very little—if not, what are the limits of its applications.

The Administration's proposal also would limit the authority of the Attorney General to delegate the right to make requests for non-individual information. Such delegation could not be made below the supervisory level of Federal prosecutors. This does have the advantage over S. 732 of removing the power from the hands of the investigative agent to one in a more responsible position and one with a broader view of the needs of law enforcement. On the other hand, the court order requirement is still lacking and, therefore, an independent review is absent.

In at least one respect S. 1891 broadens the availability of tax information over the provisions of S. 732. The Administration's proposal would permit disclosure by the Internal Revenue Service of return information to the Attorney General and redisclosure by him to a Federal intelligence agency of such information where the Attorney General certifies that the informaton sought is for use in foreign intelligence collection or a foreign counter-intelligence investigation. Such information could be furnished upon a certification that the subject of the investigation "may be furnishing or about to furnish national defense information, sensitive economic or technological information or materials, or foreign policy information to a representative of a foreign power or foreign power intelligence service." This provision seems needlessly broad and vague, subject to abuse, and unnecessary.

The provision for redisclosure of tax information to state and local law enforcement authorities is very troublesome. There are over 19,000 such law enforcement authorities in the United States, over half of which have fewer than ten employees. It would be impossible to insure the confidentiality and proper use of such information once disclosure were made.

I believe there is very little wrong with Section 6103 as it now exists. That is not to say it has operated without difficulty. There have been problems of interpretation and administration. Most of these problems have been solved as a result of experience in working with the provision and those that have not been, can be. Recent amendments to administrative rules at both the Internal Revenue Service and the Department of Justice should eliminate much of the red tape that has interfered with the effective use of these rules.

It is worth noting that while there have been criticism of the provisions of Section 6103 governing the standards to be applied in obtaining a court order for returns and return information, such a request has never been refused by a court. There has, however been little use of the provision by many United States attorneys while others have used it frequently and successfully. It would appear that an educational effort by the Department of Justice concerning the existing rules would not be out of order.

The letter from the Department of Justice to the Speaker dated November 19, 1981 transmitting the Administration's proposed amendments to section 6103 states: "This legislation would be of particular benefit in strengthening efforts to control drug trafficking and organized crime. . . ."

There is no evidence whatsoever that this proposed legislation would have any such effect. One proposing changes with the potential that these have for damaging tax administration should meet a very heavy burden of proof. This has not been done and, in my view, cannot be done.

The Internal Revenue Service has an important role in the fight against organized crime and drug trafficking. That role is to prosecute those who evade their income tax liabilities—including organized crime figures and drug traffickers who, as we know, are particularly prone to do so. But the Internal Revenue Service can fulfill this role within the context of even-handed tax administration. It should not be required to act as an arm of the Department of Justice or the Drug Enforcement Agency.

Chairman RANGEL. I thank all three of you.

You referred to potential mischief, Commissioner Kurtz, and I suppose there are so many fears that people may have that cannot be reduced to actual cases. But, could you help me in figuring out what happens to an IRS agent, whose job used to be to assist taxpayers in audits and determine what mistakes have been made and to assist him in making certain that corrections are made so that he can pay the Government what is due. The problem is what happens when, all of a sudden, this very same cooperative agent is transferred to the intelligence department, and has the same type of taxpayer before him, except he now reports to the Criminal Division? It just seems that with a provision that the IRS is required to turn over evidence of any violation of laws, it would be difficult for the taxpayer to ever find a cooperative agent.

Mr. KURTZ. Well, let me say I agree with that, Mr. Rangel. My experience with the IRS is that there are, by and large, very high caliber personnel who take their duty very seriously and will do whatever their duty requires them to do. If their duty requires them to turn over evidence of nontax crimes, that implies that they should be looking for such evidence and I think they will do it, and I think it will change the nature of the relationship in many cases between the IRS auditor and the taxpayer.

Chairman RANGEL. Well, what is really the difference between a mistake in filing a return and a criminal mistake, except intent? And now look at the agent, who is trying to make points for advancement. It is not his job to convict, but what mistakes could not be properly interpreted as a matter to be turned over to the Criminal Division?

Mr. KURTZ. You mean of tax crimes?

Chairman RANGEL. Yes.

Mr. KURTZ. Well, those judgments are made today by agents all the time. This bill, S. 732, would extend those judgments into the nontax criminal area where, I might say, revenue agents do not have experience—do not know very well the nontax criminal code and I think you would find large numbers of improper turnovers. I think you would find effort being expended to follow through what they would view as leads.

Let me just add, Mr. Chairman, this whole bill started out, as Senator Nunn said this morning, as a result of his committees concern about narcotics trafficking. Now the provisions apply primarily to corporations and foundations and labor unions, and I am not sure that it hasn't gotten so far from the original purposes that even if the original purpose might have justified some changes, which I don't think they do, this bill doesn't respond to what is claimed to be the problem.

Chairman **Rangel**. Mr. Crane?

Mr. **Crane**. I want to congratulate, first of all, all of the gentlemen for their testimony. In your testimony, Commissioner Kurtz, you indicated that there is the potential at the present time to secure court orders and that you, in your experience, were not aware of a denial, ever. Commissioner Alexander indicated the same thing, based on his experience. Commissioner Alexander, however, did indicate, and it is somewhat germane to a comment Senator Nunn made earlier, that there may be a cumbersome and time consuming procedure under existing law that might be reviewed.

Do you share that view?

Mr. **Kurtz**. Yes; I do. U.S. attorneys, by and large, do not like 6103 at all, and are very hostile to it. I appeared at a meeting, when I was commissioner, of all U.S. attorneys. Someone suggested I was taking my life in my hands to walk in and talk to them about 6103. But what came out of that meeting were a couple of problems. One is that under existing law requests under 6103 for the court order must be made out of Washington. U.S. attorneys working on a case don't like to refer matters to Washington, first of all. And second, that within the Department of Justice there are levels of review which make such applications time consuming and cumbersome.

I would have no objection at all to a change that would permit those requests to be made out in the field although at a sufficiently high level to assure that someone responsible is making the requests. There are many complaints about the standards. The claim is that it creates a catch-22 situation. I don't agree with that but, again, if there were to be some changes in the language which would facilitate the court order that would be all right as long as it continues to require that the Justice Department have an investigation underway and that the requests be specific and that there be some determination that the information sought is likely to be relevant to what they are already doing. That is essentially the standard which should be maintained.

Mr. **Crane**. Thank you very much. I have no further questions.

Chairman **Rangel**. We want to thank you.

We have to vote, and we will recess until 1 o'clock. Thank you so much.

[Recess.]

Chairman **Rangel**. The committee will resume the hearings and taking of further testimony, and we are privileged to have with us Charles H. Gustafson of Georgetown University Law Center. We thank you for your patience, and your full statement will be made a part of the record, and we can proceed as you would find convenient

STATEMENT OF CHARLES H. GUSTAFSON, GEORGETOWN UNIVERSITY LAW CENTER

Mr. GUSTAFSON. Thank you, Mr. Chairman. I want to apologize to you for not having a text of my statement for you. I talked with your staff last week and explained that I wouldn't be able to turn to the preparation of testimony until the weekend, and unfortunately Georgetown University doesn't provide weekend staff.

Chairman RANGEL. Well, we will have the record to remain open in case you want to submit written testimony.

Mr. GUSTAFSON. Thank you very much.

I appreciate the opportunity to speak with you about this difficult issue. It is a matter that has occupied a portion of my attention for a number of years. I participated in that study of the Internal Revenue Service that was undertaken through the auspices of the Administrative Conference of the United States in 1974 and 1975. I served as a consultant to the Privacy Protection Study Commission in 1976 and 1977, and I have devoted a substantial amount of time during the past few months to a fresh examination of some of the issues that are presented to this subcommittee today in connection with an independent study that has been sponsored by the Fund for Public Policy Research. I shall incorporate the results of that study in a paper that will be published early in 1982.

You have heard and will be hearing from many individuals who have been deeply involved as Government officials in various aspects of the issue of taxpayer confidentiality and the use of Internal Revenue Service files and resources for nontax purposes. You will also be hearing later this afternoon from representatives of a number of interest groups that are particularly sensitive to and concerned about various aspects of the matter. These witnesses will provide direct evidence of the impact of the provisions of the Tax Reform Act of 1976, which affected such a major change in policy with respect to the use of tax information.

I have not been involved in government during these years. I represent no particular interest group. The contribution that I would seek to offer would be to state again what I view as the specific nature of the values that here conflict and to offer my impressions, based primarily upon a close analysis of the public record that has been developed during the past 5 years, of the considerations that are relevant to your decision here.

Every witness will tell you that we have a complex question and that your responsibility is to balance properly the competing interests. One of the reasons for difficulty in the balancing act is that the competing interests are so very appealing. There is motherhood and apple pie on both sides. No one is going to speak against improved law enforcement, and hardly anyone is going to applaud publicly further invasions of personal privacy by a mammoth government equipped with the astonishing legacy of the computer age. But your decision requires a choice. It is therefore necessary to explore in more detail the nature of the interests which are at stake.

There is a practical side and a philosophical side to this question. While they are self-evidently interrelated, it is difficult to articulate the relationships. Yet, it is essential to do so. The practicalities of the question, I believe, are presented on the one hand by witnesses who assert that law enforcement is substantially impaired by the denial of information for nontax investigations and prosecutions to law enforcement officials. On the other hand, you have heard three Commissioners of Internal Revenue testify that the use of Internal Revenue Service data and resources for nontax governmental objectives creates a serious risk to the effective performance of the crucial task for which the Internal Revenue Service was established and operates, that is, the collection of revenues.

In considering this practical dilemma I have reflected upon the detailed statements that have been made on both sides which appear in the public record. That record has been developing since the mid-1970's when hearings eventually leading to the adoption of the provisions of the Tax Reform Act of 1976 were undertaken by various legislative committees. They have continued regularly, almost from the moment that the 1976 law went into effect.

One of the principal frustrations with this record is its conclusory nature. Witnesses are often able to state their bottom line views with respect to the balance that must be struck but witnesses often have trouble in articulating specifically the reasons for striking the particular balance.

Law enforcement officers have consistently and forcefully asserted their need for tax information. Some of the testimony accumulated over the last 5 or 6 years indicates that feelings were so strong that even the suggestion of denying access to IRS information was viewed as some kind of sub silentio support for organized crime and drug traffic.

It is instructive to consider the kinds of data that the Internal Revenue Service might have with respect to nontax crimes. The extraordinary storehouse of information maintained by the Service, of course, contains information of all kinds. Law enforcement officers have, however, consistently emphasized the value of IRS data, not so much in the tracking of everyday crimes—except when dramatic examples are cited—but because the data was especially helpful in the tracing of financial transactions. Tax return information helps to establish the trail of money on which many organized crime, narcotics trafficking, and other white-collar investigations are based.

But it is very difficult—from the public record at least—to ascertain with very much clarity exactly what kind of information is regularly sought. Yet, this is the crucial question. A tax return, generally speaking, reflects the consequences of transactions and money flows that have already been effected. To the extent that the returns merely reflect these transactions and this flow, the returns would not ordinarily seem to be the best available evidence of the transactions in question. But the Internal Revenue Service files might be the most easily accessible sources of information.

The Privacy Commission, in attempting to identify as accurately as possible the specific nature of information that was transferred in order to determine whether alternate sources for such information might be available, undertook, with the cooperation of the Internal Revenue Service to audit information transfers during a 3-month period in 1976.

The results of that study are set forth in the Commission's final report, which was published in 1977. The results were surprising.

Many of the items requested by law enforcement officers were easily available from alternate sources. Some were even available from the public record. But it was easier to call on the IRS files.

These findings can, of course, be subject to criticism. Knowing that a special audit of this nature was being undertaken, I recognize that it is quite possible that the months in question were not representative. Law enforcement officers may have chosen not to seek information during that period. IRS agents may have discouraged requests during that time. I have, however, found no useful data which substantially challenges the results of this particular study.

Of course, the results of the study, even if they are valid, can lead to a number of somewhat conflicting confusions, depending upon your viewpoint. One might say that, since the information isn't so special, why not provide law enforcement officers with the easiest and the cheapest access to it. In the alternative, one might say that, inasmuch as the information is available from alternate sources, why not encourage law enforcement officers to pursue the alternate sources.

The public discussion of this issue during the last 5 years, as augmented by my conversations with law enforcement officers and tax officials, indicates that there is a second aspect of this question from the law enforcement perspective. It is not necessarily addressed directly by the legislation in question. It is clear that law enforcement officers generally perceive the Internal Revenue Service as having the most fully developed expertise in financial analysis and financial investigations. Therefore, nontax investigations and prosecutions are often substantiated by the participation of IRS officers who might provide more or better expertise than would otherwise be available. Some have expressed the view that the decisions with respect to the allocation of resources within the Internal Revenue Service—toward tax administration and away from criminal nontax prosecutions—have been the most substantial impediment to criminal investigations during the past few years.

The frustrating aspect of the public record from the point of view of law enforcement is this: It is virtually impossible to ascertain the extent to which investigations were, in fact, failed because of the denial of IRS information.

Some data with respect to this has been offered. For example, it has been testified that very few requests for information have been made, compared to the period prior to 1976. It has been testified further that very few court orders have been sought. These data, it seems to me, only demonstrate that the objectives of the 1976 legislation—that is, to restrict access and to encourage the use of alternative forms of information—have been partially achieved. In fact, during testimony in 1980, a representative of the Department of Justice testified as to a series of dramatic examples when information was withheld. In almost each case his last line was, in effect, that the prosecutions continued and that the convictions were obtained, but it was harder to do so. Whether or not achievement of the objective of law enforcement has truly been impaired is another question that is not moved by the information that I have seen.

The other side of the practical issue is most sharply presented by the consistent testimony of the three Commissioners of Internal Revenue to the effect that tax administration objectives are impeded by the provision of information for nontax purposes. They cite several reasons for the conclusion. Most important, probably, is the perception that the dissemination of tax information broadly throughout the Government by the Internal Revenue Service has an adverse impact on voluntary compliance. While this adverse impact has not always been articulated in detail, I believe that it arises from the concern of the tax administrators that the public may feel a sense of unfairness about the tax system. To the extent that the public perceives that the structure and/or the administration of the tax system is unfair, voluntary compliance will necessarily be diminished.

One response to this view has been along the lines that a law abiding taxpayer shouldn't be concerned about the provision of information to other agencies." One witness at hearings on this subject conducted earlier in the fall pointed out, in fact, that the degree of voluntary compliance by taxpayers generally has diminished substantially during the past 5 years. I think one would be hard-pressed to support the proposition that the disclosure limits set by the 1976 Tax Reform Act have generated massive noncompliance.

On the other hand, it is true that there has been no attempt and it is possible that no successful attempt can be made to quantify the real impact on voluntary compliance as a result of IRS disclosure policies. It should be noted in this context, however, that the Congress has been extremely sensitive to the question of voluntary compliance with information gathering processes in other contexts. The information accumulated by the Census Bureau, for example, is made available to virtually no other Government agency.

With respect to the practical aspect of the question, then, there is an absence of useful data on both sides. There is no reason to believe that everyone is not telling at least a measure of the truth. Unfortunately, this does not materially advance your decisionmaking process. But an analysis of the philosophical aspect of the question is useful in approaching the evaluation of the practical considerations.

From the law enforcement side the argument is straightforward. The information already exists. It has been assembled for legitimate governmental purposes. Since it is already extant, there is no serious further intrusion upon the privacy interests of the individuals affected. In fact, some argue that it is almost silly for the Government to decline to use information for serious objectives that has already been acquired and filed away in the governmental data banks.

On the other side, of course, is the peculiarly intangible question of privacy. The argument runs that the mere existence of the data is not a reason to authorize its usage. First, the information only exists because of a system of revenue collection that compels citizens to disclose information about themselves and about others and which authorizes the tax collector to exercise extraordinary powers of information collection with respect to all citizens.

The importance of revenue collection to a free government has been the basis for constitutional distinctions in interpreting aspects of the tax collection system. Thus, while generally a witness cannot be compelled to testify against himself, the Supreme Court has consistently sustained the constitutionality of the compulsion to report, which is part of the tax system even though criminal consequences can attend the failure to do so. Moreover, extraordinary collection powers on the part of the Internal Revenue Service have been sanctioned by the Supreme Court in situations where preattachment hearings would normally have been required as a constitutional necessity. Again, the justification for these decisions lies in the judicial recognition of the crucial role that revenue collection plays in the ability of our Government to continue to function.

Concern for normal criminal law enforcement has not been similarly blessed. The result is that to the extent the extraordinary powers of the tax collector are employed for objectives that are not inherent in the tax collection process, the constitutional and the philosophical impediments to the accumulation of information and the use of legal compulsion in the gathering of information by the Government are, at least in one sense, quite clearly circumvented as well. Whether such circumvention is appropriate is the essential question that is raised by the proposed legislation.

The values which in here in the constitutional limitations on information gathering and the use of compulsion to illicit data and which in here in our concern for privacy are obviously worthy ones. My own judgment is that the importance of these values serves as a mark in approaching the question of practicalities. They lead me to conclude that in effecting the difficult balancing task that is so often described to you, a burden of proof with respect to the practical considerations must be allocated to the side who would impinge on the values of privacy. Having reached that conclusion I look back to my analysis of the testimony in support of greater access. The record appears to me to be a modest one.

Fortunately, the purpose of these hearings is further to develop that record. I have suggested here a way of breaking down the practical and the philosophical considerations. I urge you, in developing further a factual record upon which the balance can truly be struck to press hard for specific information about the kinds of nontax crimes that are being fostered by denial of access, the specific nature of the evidence that exists only in the Internal Revenue Service files; the avenues that are really available to gather evidence from alternative sources; and the reasons why the modest requirement of a judicial order in certain cases is so unworkable.

I would urge further that to the extent possible the question of allocating Internal Revenue Service resources to nontax criminal investigations be treated as a somewhat separate question. I do share the evolving consensus that the Internal Revenue Service is today confronted with problems of enormous dimensions and I share the impression that public respect for the tax system is diminishing.

Chairman RANGEL. Professor, I am reluctant to interrupt, but we do have a long list of witnesses that we hope to be able to call this afternoon, and I hope you will be able to conclude your observations.

Mr. GUSTAFSON. I shall do that.

Finally, I have a few comments on the specific aspects of the proposed legislation. There are two elements that are, in my view, supported by the record to date. To the extent that the appropriate safeguards, whatever they are determined to be, can be administered without involving higher Government officials, the procedure should be implemented at more local levels. But and the process should be audited carefully.

Also, where nonwillful violations of the disclosure laws are made by Government officials, the approporiate civil remedy should be against the agency in question rather than the individual officer.

I have one overwhelming and important impression to offer about the remainder of the proposal. I believe that it fails to reflect the practical realities of the Internal Revenue Service data collection process. The operating reality is that pieces of information gathered by the Internal Revenue Service pursuant to its extraordinary powers do not segregate themselves and identify themselves easily. They are thoroughly mixed in the tax files and to legislate in the belief that it is easy to distinguish one kind of information from another is likely to lead to inappropriate legislation.

Finally, it is easy to understand the desire of all those who ask for increased access to assert that it constitutes an appropriate balance between privacy and access. As I have said, the operating reality is that your decision requires a choice between the two. I think that there is a serious risk that the Internal Revenue Service files are going to be reopened for virtually all relevant information as a result of the legislation that has been proposed here.

One of the worst aspects of it will be if the Congress decides to reopen even those files while misleading itself and/or the public about the decision that is in fact being taken. If a determination is made that the objectives of law enforcement merit further intrusion on the privacy interests of individuals and possible adverse impact in revenue enhancement, then I urge that it be express and clear so that the public and so that the Government agencies that are affected will be able to understand and to administer the legislation.

Thank you.

Chairman RANGEL. Thank you, Professor, for your contribution and the guidelines that you have given to our committee as we prepare to review this very sensitive legislation, and we certainly hope to be calling upon you in the future. Thank you for appearing with us.

The American Civil Liberties Union, John H. F. Shattuck, the national legislative director. He will be accompanied by Wade Henderson, the legislative counsel.

STATEMENT OF JOHN H. F. SHATTUCK, NATIONAL LEGISLATIVE DIRECTOR, AMERICAN CIVIL LIBERTIES UNION, ACCOMPANIED BY WADE J. HENDERSON, LEGISLATIVE COUNSEL

Mr. SHATTUCK. Thank you very much, Mr. Chairman. We also have a very lengthy statement which we will submit for the record. I hope it will be included for the record. I will summarize and refer to portions of it.

Chairman **Rangel**. Without objection.

Mr. **Shattuck**. Mr. Chairman, this is an extremely important subject and one which we have had the privilege of appearing before your committee and other committees of the Congress on in the past.

The disclosure and summons provisions of the Tax Reform Act are the product of a grave concern for the privacy of tax records held by the IRS. Central to the origins of these provisions were the extensive revelations of abuse of IRS. Information by other agencies of the Government which had solicited that information from IRS. While the most sensational and well-publicized of these abuses occurred during the Watergate period, we are dealing with a much larger and more extensive record which goes far back in time and a record which the Tax Reform Act addresses directly.

Let me give you a few examples from our prepared statement, Mr. Chairman. Between 1966 and 1974 the FBI either directly or through the Justice Department made approximately 200 requests to the IRS for tax returns. Sixty-five percent of these requests were for two counterintelligence programs conducted by the FBI, the so-called key activists program aimed at leaders of the anti-Vietnam war movement and the key black activists program aimed at the leaders of the so-called Black Nationalist movement.

In addition, the FBI made numerous ongoing requests to the IRS for lists of contributors to ideological organizations under investigations by the Bureau in this manner, the FBI obtained information provided voluntarily to the IRS by taxpayers to assist in the enforcement of the tax laws.

Another agency, the CIA, between 1957 and 1972 also made a large number of unofficial requests to IRS for tax return information on persons the CIA was investigating. Before the 1976 Tax Reform Act, as the Congress has found and as several responsible committees of the Congress have determined in extensive investigation, the IRS was a beleaguered agency lacking any meaningful standards by which to judge the numerous requests that were coming to it from many other agencies of the Government.

It didn't want to fill those requests but it didn't know what to do about them until the Congress finally got in the act to try to protect the integrity of the agency.

While a procedure for determining the legitimacy for requests in the IRS did exist, it was so vague as to be virtually useless, and in 1968 when the chief of disclosure of IRS learned of the procedure, he termed it illegal. The act was designed to remedy this problem. It is by no means stringent. It provides protection of information and permits disclosure of information for investigative purposes. Disclosure may only be made following the independent judgment of the Federal judiciary.

I should say at this point, as you probably know, Mr. Chairman, that the 1976 law is, by no means, as stringent as many responsible people in the Congress and the Privacy Protection Study Commission recommended. It is a compromise and it provides for disclosure as well as protection.

A person's tax records and the records of his financial transactions with the bank or other private entities are a reflection of that person's life. These records mirror in great detail the personal habits and associations of individuals.

In 1975, Commissioner Alexander, whom you heard from this morning, testified before this committee that the IRS has a "gold mine of information about more people than any other agency in this country." And he was right. And the IRS has always sought to protect that information, but in many instances it has had a great deal of difficulty resisting the pressures from outside.

Congress has given the IRS extremely broad coercive powers to obtain information from individuals about every aspect of their private lives, and those powers are very important in the collection of taxes. Without a subpena or a search warrant or any showing of probable cause the IRS may require an individual to divulge almost anything. Because of the clear threat that those powers hold to an individual's constitutional rights, the courts have carved a very narrow exception to the fifth amendment for the benefit of the IRS. This exception, and the authority which Congress has given the IRS, creates, I think, a very powerful presumption against any attempt to transfer that authority to other agencies of the Government, and that is why the Tax Reform Act was enacted.

Senator Nunn this morning, and other proponents of this legislation, criticized the low level of participation by IRS in the battle against organized crime. But in our view that casts the issue in the wrong light. The IRS is not supposed to be a central participant in that battle. Its great powers were given to it for another extremely important purpose, a purpose which would result in the shutting down of the Government if it weren't properly performed, and that is the collection of revenue.

Now, in order to promote efficient tax administration as the Commissioners have told you in their testimony, it is essential not to burden the filing of taxpayer returns with fifth amendment problems. If a taxpayer believes that the information he or she is providing to the IRS might be routinely made available to other agencies of the Government, he might be less disposed to be cooperative with the IRS. The taxpayer would be put in the position of having to scrutinize everything that was provided voluntarily and to determine whether that information might be relevant to any possible criminal investigation that the Government might seek to initiate. And if, as a result of that taxpayer guesswork the taxpayer then decided to claim a fifth amendment privilege for fear of losing the privilege otherwise at a later stage, the process of tax collection would be made so complex and so burdensome and so cumbersome as to render it virtually ineffective.

Mr. Chairman, I have just gone briefly through these background questions of constitutional policy because I think they provide the framework within which your subcommittee must look at any proposals to change the Tax Reform Act. We are fundamentally opposed to any changes in that law because that law has been hammered out as a very reasonable compromise which addresses many of the concerns on the one hand of limiting the disclosure of information by IRS and, on the other hand, of providing some means within which the investigative requirements of the Government can be fulfilled.

Let me highlight the specific objections that we have laid out in our testimony to the proposals facing the subcommittee and also which are being aired, as you know, elsewhere in the Congress.

First, is the proposed change in the definition of protected information so that nothing except the information that actually appears on the face of the tax return would be protected against disclosure for nontax investigative purposes. This change, if it were to be made, would virtually eliminate much of the protection that is now set out in section 6103. A comment to this proposed change suggests that it is intended to separate those items which deserve a higher degree of privacy and hence a court order for disclosure of items that IRS, like other agencies, typically uncovers in an investigation.

We think this is very misleading because it is by no means clear that the information on the tax return is the only information deserving of a high degree of privacy. There is plenty of other information that taxpayers provide in connection with an audit or which IRS retains in connection with its summons procedures which is at least as important, and I think Senator Nunn himself testified this morning that a great deal of the nontax return investigative information is of even more interest to the Government than tax return information.

The proposed new definition of protected information also draws, we think, an unwarranted distinction between an individual's tax return and a corporation's tax return—apparently on the assumption that a corporation's return does not contain sensitive information concerning individuals. Such a premise is unjustifiable. A corporation's tax return can reflect all kinds of personal information. A person's stockholdings; how he or she voted on internal matters; and confidential communications between the corporation and the individual. It may even get to the point that the officers of the corporation are the subjects of an investigation and the corporation's tax records are going to be very useful to that investigation and if they are routinely available pursuant to the lower standards of the proposal, then we think there is a severe curtailment of the constitutional rights of those corporate officers.

The second change that we oppose is a lowering of the standards of proof that a Government agency must meet in order to obtain access to taxpayer information. The act now requires a showing that there is reasonable cause to believe that a specific criminal act has been committed. The information sought is probative evidence of a matter related to that criminal act and the information cannot be obtained elsewhere. If those three conditions can be shown, then judicial disclosure is perfectly appropriate.

While the reasonable cause language is retained in the proposed legislation, the bills would effect several very serious changes in this area. They would eliminate the requirement that the information be "probative evidence of a criminal act" and substitute a lower requirement that it "may be relevant to a criminal investigation," and it would also eliminate the requirement that the information can't be obtained elsewhere. This would virtually eviscerate, we think, the basic protections that are set out in the court order procedure.

These standards would open up tax records of innocent taxpayers to a wide variety of new investigative uses. I use the term innocent intentionally here because I think, for example, if the Department of Justice were engaged in an ongoing investigation of a suspected criminal enterprise as defined in the bill, the proposed standards would allow the Department to gain access to tax records of any individuals innocently associated in any way with that enterprise. It could be argued that this is necessary in order to cast the investigative net as broadly as possible, particularly in the investigation of drug trafficking and organized crime, but it is pretty disturbing to think that anyone associated with an enterprise that is the subject of an investigation, even if that person is in no way part of the enterprise, would have their tax records routinely made available under this lower standard.

The third change that we oppose, Mr. Chairman, is the imposition of a new requirement on IRS to disclose "to the appropriate Federal agency" any nonreturn information which may constitute evidence of the violation of Federal criminal laws. This is, as several other witnesses and as the IRS Commissioners have testified, a virtual fishing expedition invitation and a terrible burden on the IRS, which would be required to search their records constantly to find out whether there is anything in there which may constitute evidence of the violation of the Federal criminal laws. It is hard to imagine how IRS could perform its normal tax investigative function if this kind of administrative burden is to be imposed on it.

The fourth area that we are concerned about is the new authority that the legislation would provide to allow routine dissemination to State agencies, some 19,000 of which would be authorized to receive this kind of information, without any further checks on its use.

The fifth concern we have is the proposal to allow foreign governments to obtain tax information routinely, assuming that there were some treaty obligations that made that possible, and what we are worried about in this instance is that the laws of a foreign country may be very different from the laws of the United States, and what might be a crime in Uruguay may not be a crime in the United States. Making routine tax information available under those circumstances is a major privacy setback, and also an imposition on the powers of IRS.

A sixth area which has just emerged in these proposals which concerns us, and I would think would concern you very much, is the proposal to allow the routine dissemination of taxpayer information sought for use in foreign intelligence or foreign counterintelligence investigations, not further defined anywhere in the proposals.

This we think is a particularly dangerous proposal, and it deserves the most serious and probing scrutiny by this subcommittee.

Its overbreadth could trigger a disclosure of tax information of citizens engaged in the most benign kind of international activity, and we think its chilling effect on speech and various kinds of exchanges of technological information could be devastating.

It is vague, sweeping, and appears to us to be a back door effort to gather further authority for foreign intelligence agencies in the context of legislation which is not aimed at that purpose whatsoever, and which has no business being in this proposal.

Finally, Mr. Chairman, I will conclude on something of a positive note by saying that we do support some of the proposed changes that would streamline the procedures of existing law, assuming that there are no basic changes in the standards of existing law.

We endorse the imposition of time limits, the extension to magistrates of the authority to rule on Government applications and the provision allowing attorneys for the Government rather than the heads of agencies to apply for disclosure.

If these administrative changes are made, they would, in fact, make it much easier for the law to be used. We think there is a serious problem of the education of U.S. attorneys around the country about the availability of the procedures which they can use under current law.

If these streamlining arrangements are adopted, then we think current law would be perfectly adequate to serve the purposes for which it was originally enacted and will, at the same time, provide the basic protections which the 1976 law provided.

Mr. Chairman, we are delighted to be here and to help you in any way we can to answer any of your questions and to provide any additional information that you might want for the record.

Thank you very much.

[The prepared statement follows:]

STATEMENT OF JOHN H. F. SHATTUCK, NATIONAL LEGISLATIVE DIRECTOR, AND WADE J. HENDERSON, LEGISLATIVE COUNSEL, AMERICAN CIVIL LIBERTIES UNION

We are pleased to testify this morning on the privacy of taxpayer information, an issue of much importance to the American Civil Liberties Union. I am the Legislative and Washington Office Director of the ACLU, a nationwide, nonpartisan organization of more than 250,000 members devoted to the protection of individual rights and liberties under the Constitution. I am also the author of a textbook, "Rights of Privacy" (National Textbook Co. 1977). With me today is Wade Henderson, Legislative Counsel in the Washington Office of the ACLU.

For many years the ACLU has played an active role in the effort to safeguard individual privacy from broad intrusion by government and private recordkeeping practices. Through a project on privacy and data collection which we sponsored from 1973 through 1978, the ACLU provided advice—and in some instances legal representation—to individuals whose rights and interests were adversely affected by the recordkeeping and dissemination practices of governmental and private institutions. We also sought to publicize in a monthly Privacy Report the many ways in which privacy has been eroded in a society which personal information is increasingly recorded by third parties and used for a wide variety of purposes, without the consent or even the knowledge of the person involved.

The ACLU is particularly concerned about the issue of taxpayer privacy, and has testified frequently in congressional and other hearings on this subject, including hearings of this committee when it was considering the Tax Reform Act of 1976; and last year when it considered a bill similar to the one under consideration today. We were strong opponents of the Justice Department's earlier effort to amend the Act in 1977, and we oppose many of the proposed amendments before the Committee today.

PRIVACY OF TAX RECORDS

The disclosure and summons provisions of the Tax Reform Act of 1976 are the product of a grave concern for the privacy of tax records held by the IRS. The provisions were generated by revelations, over a period of several years, of a widespread pattern of abuse of IRS records by government agencies for non-tax purposes. Among the many improprieties that were revealed by various investigations of governmental intelligence operations were a number of projects initiated within the IRS as a result of pressure brought to bear on that agency by governmental law enforcement agencies. These projects included the Ideological Organizations Audit Project and the Special Service Staff (1969–73) which targeted more than 8,000 individuals and 3,000 groups for extensive investigation specifically because of their political activities. The SSS operated in secrecy and was abolished in 1973 when IRS Commissioner Donald Alexander learned of its existence. These internal IRS projects seriously threatened the contitutional rights of all taxpayers. The projects were the product of external pressures exerted by Congress, the White House and government law enforcement agencies who claimed that the IRS was not participating sufficiently in the governmental battle against crime.

More central to the origins of the disclosure provisions of the 1976 Act were the extensive revelations of abuse of IRS information by other agencies of the government which had solicited the information from the IRS. See Final Report, Book III, Senate Select Committee on Study of Governmental Operations with Respect to Intelligence Activities, 94th Cong., 2d. Sess. [Church Committee] (1976). Between 1966 and 1974, the FBI, either directly or through the Justice Department made approximately 200 requests to the IRS for tax returns. 65 percent of these requests were for two counter-intelligence (Cointelpro) programs conducted by the FBI—the Key Activist program aimed at leaders of the anti-Vietnam War movement, and the Key Black Activist program, aimed at leaders of the so-called Black Nationalist movement. In addition, the FBI made numerous ongoing requests to the IRS for lists of contributors to ideological organizations under investigation by the Bureau. In this manner, the FBI obtained information offered voluntarily to the IRS by groups to assist in enforcement of the tax laws. Between 1957 and 1972, the Central Intelligence Agency made a number of unofficial requests to the IRS for tax return information on persons the CIA was investigating.

Finally, the Senate Committee that investigated the Watergate burglary revealed extensive use of IRS records by the White House against political opponents of the Nixon Administration. Indeed, abuse of tax information was one of the central components of the Nixon Administration's broad pattern of intelligence operations aimed at harassing and intimidating political "enemies."

Before the Tax Reform Act of 1976, the IRS lacked any meaningful standards by which to judge the numerous requests for information it received from other government agencies. Though a procedure for determining the legitimacy of requests did exist, it was so vague, and so widely ignored as to be useless. Indeed, in 1968 when the Chief of Disclosure of IRS learned of the procedure, he termed it "illegal." The Church Committee found that in the absence of any meaningful guidelines, the IRS could not judge whether the request was legitimate. Consequently, the Committee noted, the "IRS had delegated the determination of the propriety of the request to the requesting agency." Final Report, Senate Select Committee to Study Government Operations. With respect to Intelligence Activities, Book III, p. 840.

The Tax Reform Act was designed to remedy this legacy of abuse of IRS information. Although the Act is by no means stringent, it provides a degree of protection of IRS records. It requires the government to meet a reasonable standard of proof to justify disclosure. Furthermore, such disclosure may only be made following the independent judgment of a federal judge. These safeguards were all designed with specific reference to known abuses of IRS information by government agencies.

It is important to remember as well that the Tax Reform Act was intended to correct a chilling pattern of abuse by the IRS established long before the Watergate revelations. While Watergate was undoubtedly a catalyst in the movement for the reform of tax disclosure procedures, to characterize the Act as merely a "post-Watergate" reform is short-sighted and misinformed. The history of broad IRS involvement in improper disclosure activities prior to Watergate rendered the effort in 1976 to limit such activity all the more urgent. The Tax Reform Act was not directed at mere aberrational abuses from a brief period to the history of the agency; it was designed to restore the IRS to its original and only proper government function.

SENSITIVE NATURE OF TAXPAYER INFORMATION

A person's tax returns, and the records of his financial transactions with a bank or another private entity, are a reflection of that person's life. Those records mirror, often in great detail, the personal habits and associations of individuals. The beginning of a tax return gives name, address, social security number, indentity and dependents and the taxpayer's gross income. Various schedules may indicate political and religious affiliations and activities, medical or psychiatric treatment, union membership, creditors, investments and holdings. Additional documents compiled by the taxpayer and pertaining to statements made on a tax return but not filed with the return contain a similar wealth of sensitive personal information. In 1975, the then IRS Commissioner Donald Alexander noted that the IRS has a "gold mine of information about more people than any other agency in this country." Committee Print, Confidentiality of Tax Returns, House Committee on Ways and Means, September 25, 1975, at 3.

Apart from information related to tax returns, documentary materials routinely obtained by IRS for the enforcement of the tax laws also contain vast quantities of private information. Bank records, or similar records, reveal the political causes one supports, the books and magazines one buys, the organizations one joins, as well as one's style of life, tastes and habits. People assume that these matters are confidential, and that they do not sacrifice that confidentiality when they conduct financial transactions with the assistance of a bank. This assumption has been acknowledged and embraced by courts across the country. As one state court has noted: "[I]t is impossible to participate in the economic life of contemporary society without maintaining a bank account. In the course of such dealings, a depositor reveals many aspects of his personal affairs, opinions, habits and associations. Indeed, the totality of bank records provides a virtual current biography." *Burrows* v. *Superior Court*, 13 Cal. 3d 238, 529 P.2d 590 (1974).

We make these opening observations so that it is clear that the privacy interest an individual has in his or her tax return and bank records is formidable, and must be taken fully into account. Last year, in introducing proposed amendments to the Internal Revenue Code similar to those under discussion today, Senator Nunn noted that "a balance must be struck between the privacy of tax returns and the legitimate needs of law enforcement agencies." Congressional Record, March 11, 1980, p. S2375. The hearings that generated these bills contained testimony principally from law enforcement officials concerning the asserted needs of law enforcement agencies. If the balance to which Senator Nunn referred is to be struck fairly and accurately, it is essential that the privacy interests of individuals be given equal weight.

THE EXTRAORDINARY POWERS OF IRS

The IRS is accorded enormous, unparalleled coercive power to obtain information from individuals concerning every aspect of their private lives. The IRS may, without a subpoena or a warrant or any showing of probable cause, require and individual to divulge information. Because of the clear threat such broad powers hold to an individual's constitutional rights to be free from government coercion, the Supreme Court has carved a narrow "required records" exception to the Fifth Amendment, principally for the benefit of IRS. See *United States* v. *Sullivan*, 274 U.S. 259 (1927). This exception and the extraordinary authority which Congress has bestowed on IRS create a powerful presumption against any attempt to transfer that authority to other agencies of government.

The statutory authority of IRS to obtain information must not be viewed as creating some form of governmental asset which may then be transferred to other arms of the government pursuing legitimate governmental objectives. The information gained by the IRS does not in any sense "belong" to the government. Rather, it is held in special trust by the IRS for its unique, important purpose of collecting taxes. Indeed, it is only the unique nature of the IRS function that justifies the extraordinary degree of intrusion that that agency is allowed to make into the lives of individuals. Dissemination of IRS information to other governmental agencies for non-tax purposes, however meritorious, is a violation of the IRS' special trust.

The insufficient level of participation of IRS in the government battle against organized crime and large drug trafficking has been cited as the central concern with current law. In our view, casting the question in that light fundamentally distorts the realities of the situation. The IRS is not designed to participate in that battle. Its extraordinary powers were granted for quite another purpose—the collection of revenue and enforcement of tax laws—and are limited to that purpose. To the extent that the IRS has, in the past, strayed from that purpose, it has operated outside its charter. Measures taken to remedy that impropriety are to be lauded; to portray the Tax Privacy Act of 1976 as withdrawing the IRS from the battle against crime is misleading and harmful.

Governmental agencies such as the Department of Justice, the Drug Enforcement Administration and the Federal Bureau of Investigation are not—and should not be—empowered to exercise the same authority as the IRS to compel and use personal records and other information about virtually the entire public. As the Privacy Protection Study Commission noted in its 1977 report: "It is understandable that other agencies with important responsibilities want to use information the IRS has authority to collect, but they have not, in fact, been vested with the IRS' authority to compel such information." [Report at p. 540.]

We believe that dissemination of taxpayer information and records by IRS to other government agencies, and the summoning of financial records by IRS threaten the constitutional policy underlying the Fifth Amendment right to be free from compulsion of self-incriminating statements.

The Fifth Amendment protects an individual from government coercion in a criminal prosecution. In most instances, the government may not compel an individual to divulge information that might tend to incriminate him. The "required records" exception of the Fifth Amendment was created in part to allow the IRS to require individuals to divulge information that might otherwise be protected by the privilege against self-incrimination. Failure to provide information sought by the IRS is a felony punishable by statute (26 U.S.C. § 7602). Alternatively, the government may issue a summons to the taxpayer or to third parties that will yield information to the IRS. In either case, the information is effectively obtained by IRS through compulsion. The use of that information in a non-tax criminal proceeding, therefore, is sharply at odds with the constitutional policy underlying the Fifth Amendment.

In order to promote fair and efficient administration of the revenue laws and collection of taxes, it is essential not to burden the filing of taxpayer returns with Fifth Amendment problems. If a taxpayer believed that the information he or she was providing to IRS might be routinely made available to other law enforcement agencies, he or she might be disposed to be less cooperative with IRS. The taxpayer would be put in the position of having to scrutinize all of the revelations on the return and determine their relevance to any possible criminal investigation. If as a result of this guesswork, the taxpayer determined the possibility of self-incrimination, he would, at that time, claim a Fifth Amendment privilege, for fear of losing it otherwise at a later stage. See *Garner* v. *United States*, 424 U.S. 628 (1976). This process would make the tax collecting process so complex and so cumbersome as to render it fundamentally ineffective. The Privacy Commission expressed concern for this result in noting that "widespread use of the information a taxpayer provides to the IRS for purposes wholly unrelated to tax administration cannot help but diminish the taxpayer's disposition to cooperate with the IRS voluntarily. . . . Such a tendency in itself creates a potentially serious threat to the effectiveness of the federal tax system." Report of the Privacy Protection Study Commission, p. 540.

These impediments are unjustified. Moreover, they are unnecessary. The number of potentially valid Fifth Amendment claims would be small in comparison with the total number of people filing returns. The more practical solution is to allow the tax return process to go unimpeded by Fifth Amendment considerations—and that is precisely why the "required records" exception to the Fifth Amendment was created, and why it was limited to circumstances such as revenue collection.

These board questions of constitutional policy concerning the disclosure and dissemination of tax information provide the background against which the specific amendments under discussion today must be viewed. Because the IRS has been accorded special and extraordinary powers, we are fundamentally opposed to any dissemination of tax information within the government. If, in some extraordinary case, such dissemination is authorized by state, we believe it is essential that in order to justify it, the government must meet a high burden of proof. From this perspective, we are not satisfied with section 6103 as currently written, but we strongly oppose any attempt to further dilute its protections of taxpayer privacy.

Moreover, the need for relaxed standards of disclosure beyond the provisions of current law has not been justified. No empirical evidence has been offered to demonstrate that the relatively permissive disclosure provisions of the Tax Reform Act have not worked well in practice, nor that U.S. Attorneys who utilize the court-order procedures of the law have not been able to obtain tax records which are probative evidence of crime. For this reason, in addition to our strong support for the principles behind the Tax Reform Act, the ACLU remains unalterably opposed to any change in current law.

We will now highlight the specific objections we have to several proposed amendments currently under consideration in the Congress. Where possible we will also pose additional questions which we believe the subcommittee should press before considering other proposals for change in current law.

NARROWING OF THE DEFINITION OF PROTECTED TAXPAYER INFORMATION

Under provisions of S. 732, introduced by Senator Nunn, the current three-tier classification of IRS information would be collapsed into two categories. This change would substantially diminish the protection afforded the information in IRS records. Under existing law, the government must obtain a court order to gain access both to taxpayer returns and to what is called "return information." The latter category includes any information the IRS collects or obtains from the taxpayer with reference to the return. Such information might include documents substantiating claims for deductions, contributions or related expenditures. Current law protects this information with the court order requirement precisely because it is at least as sensitive as the information on the face of a return.

Under the proposed two-tier classification scheme of S. 732 any taxpayer information or documents which are not taxpayer returns would be available to the government upon receipt of a written request by an attorney for the government. No independent judicial check on these disclosures is required. Moreover, the bill places on the IRS an affirmative duty to disclose any such information to the government which may be pertinent to a federal criminal investigation.

We submit that this change in definitions eliminates much of the protection of section 6103. The comment to the proposed change suggests that the bill will enable the Congress to separate those items which deserve a higher degree of privacy and hence a court order for disclosure, from those items that IRS, like any other investigative agency, uncovers in a typical investigation. This is misleading. It is by no means clear that the information on the return is the information deserving of a higher degree of privacy. Indeed, there is good reason to believe that other information complied and maintained by IRS is of an even more private nature.

The proposed new definition of protected taxpayer information draws a distinction between an individual's tax return and a corporation's tax return, apparently on the assumption that a corporation's return (consisting of more than two owners or shareholders) does not contain sensitive information concerning individuals. Such a premise is unjustifiable. A corporation's tax return can reflect a person's stock holdings, how he or she voted on internal matters and confidential communition between the corporation and an individual.

S. 1891, introduced by Senator Roth, would similarly reduce the protections afforded information in IRS records. "Investigative return" and "investigative non-return" information would replace the present three-tiered classification. The bill also imposes an affirmative duty to disclose any information which may be pertinent to a federal criminal investigation, and makes a similarly unjustifiable distinction between the individual and the corporation regarding protected taxpayer information.

We note, however, the bill's selection of terminology. The use of the term "investigative" to characterize any definition of taxpayer information is, itself, a subtle reminder of the abuses which preceded current law. Such terminology carries with it the implication that the IRS is an investigative arm of law enforcement. This is a distortion of the IRS's true function.

STANDARDS OF PROOF

Both S. 732 and S. 1841 would substantially lower the standards of proof that a government agency must meet in order to obtain access to taxpayer information.

Prior to the enactment of the Tax Reform Act, the Privacy Commission recommended that when another government agency requests taxpayer information from IRS, the taxpayer be given notice, and an opportunity to contest the disclosure. Disclosure could then be authorized by a court only if it found: (*a*) probable cause to believe that a violation of civil or criminal law has occurred; (*b*) probable cause to believe that the tax information requested from the IRS provides probative evidence that the violation of civil or criminal law has occurred; and (*c*) that no legal impediment to the applicant agency acquiring that information sought directly from the taxpayer exists. Report of the Privacy Protection Study Commission, pp. 553–4.

The Tax Reform Act clearly fell short of these proposed safeguards. An ex parte proceeding requiring a demonstration of reasonable cause is considerably less rigorous than an adversary proceeding demanding probable cause. Further, the third consideration, that no legal impediment exist to direct solicitation from the individual, was overlooked altogether.

The proposal in S. 732 would further undermine taxpayer privacy by eliminating altogether the requirement of a court proceeding, or demonstration of reasonable cause with respect to the disclosure of non-return information. Substituted for these safeguards would be the word of the government attorney that the information sought is material to an ongoing investigation. In short, the proposed legislation eliminates any protection of tax information held by the IRS, other than the tax return itself.

S. 732 also reduces the standard of proof required to justify issuance of an ex parte order for dissemination by the IRS of the actual tax return. We oppose this further erosion of taxpayer privacy protection.

Section 6103 of the Tax Reform Act now requires a showing that there is reasonable cause to believe that: (*a*) a specific criminal act has been committed; (*b*) the information sought is probative evidence of a matter related to that criminal act; and (*c*) the information cannot be obtained elsewhere.

Again, these statutory standards fall short of the Privacy Commission recommendations. However, S. 732 would further reduce the safeguards. Under S. 732, the government need show only that: (*a*) there is reasonable cause that a specific criminal act has been committed; (*b*) the information is sought for an investigation concerning such act; and (*c*) there is reasonable cause to believe that the information sought may be relevant to a matter relating to such investigation.

While the "reasonable cause" language is retained, the bill effects several changes damaging to taxpayer privacy. There is no requirement that the information be "probative evidence of a criminal act"—only that it "may be relevant" to a criminal investigation; and there is no requirement that the information be otherwise unobtainable.

These lower standards would open up tax records of innocent taxpayers to a wide variety of new investigative uses. For example, if the Department of Justice were engaged in an ongoing investigation of a suspected criminal enterprise, the proposed standards would allow the Department to gain access to tax records of any individuals innocently associated in any way with that enterprise. While it may be argued that the focus of the amendment is on drug trafficking and organized crime, it is too easy to forget that similarly loose standards created the enormous record of abuses of IRS disclosures prior to the enactment of the Tax Reform Act.

In this regard, S. 1891 is a substantial step back from even the limited protections found in S. 732. In addition to similar reductions in the standards of proof found in S. 732, S. 1891 would permit the application for an order to disclose tax information based on a reasonable cause to believe that a specific criminal act "will be committed". The use of such a nebulous, conspiracy-based standard virtually insures the abuse of "investigative" discretion. It is a sweeping license to search with only the most limited judicial review. It is a threat to the privacy rights of all citizens.

There is little factual documentation of the need for these changes in the standard of proof in the Tax Reform Act. When asked to supply such information, the General Accounting Office was unable to do so. In fact, in March 1979 the GAO issued a study of the disclosure and summons provisions of the Tax Reform Act, which concluded that "the adverse impact on coordination between IRS and other members of the law enforcement community as a result of the disclosure provisions has not been sufficiently demonstrated to justify revising the law." Report by the Comptroller General, Disclosure and Summons Provisions of 1976 Tax Reform Act—Privacy Gains and Unknown Law Enforcement Effect, March 12, 1979. Not only are the good intentions of the sponsors inadequate to justify legislation of such potentially harmful consequences, but there is no clear evidence that the proposals would achieve their intended goal.

DUTY OF IRS TO DISCLOSE

The Senate bills would make a major change in existing law by requiring IRS to disclose "to the appropriate federal agency" any non-return information which "may constitute evidence of a violation of federal criminal laws." Under current law IRS is not mandated to make such disclosures and the burden is on the investigating agency to initiate a written request or court order procedure. The proposed change makes IRS an active participant in non-tax investigations and thereby substantially undermines the integrity of its tax information gathering procedures. Moreover, the burden placed on IRS of constantly searching its records to determine if they "may contain evidence of crime" is unreasonable, unworkable and wasteful of administrative resources.

REDISSEMINATION

Neither Senate bill contains a check on the chain of dissemination of taxpayer information within the government. Indeed, S. 732 explicitly provides that: "An agency head, an I.G., or the A.G. or his designee may further disclose non-return information to such federal personnel or witness as he deems necessary to assist him . . ."

The comment to the bill notes that this provision is almost identical to the grand jury secrecy rules. This comment overlooks the crucial fact that in grand jury proceedings, the government cannot compel self-incriminating testimony, at least without a grant of immunity. Since the fundamental issue here is the use of information that is coerced without a grant of immunity, the analogy the comment draws is inappropriate.

The government must meet an extraordinarily high burden to justify dissemination. Once that burden is met at the outset, the removal of all barriers to further dissemination is not justifiable. We suggest that in effect, walls be placed at every step of the process so that highly sensitive information not be disseminated throughout the government on the judgment of the government attorney.

DISSEMINATION TO STATE AGENCIES

Both S. 732 and S. 1891 provide for disclosure of IRS Information to state law enforcement officials if the information is relevant to investigation or prosecution of a state felony. This proposal is flatly at odds with a Privacy Commission recommendation that disclosure of tax information to the states was sufficiently concerned about the potential for abuse that exists in inter-governmental disclosure, that it suggested limitations even on tax related disclosure. Commission Report, pp. 546–47. Dissemination of tax payer information is an extraordinary invasion of the privacy of individuals, justified only in extraordinary circumstances. The provision allowing dissemination to state agencies is not justified by such circumstances. Rather, it treats intergovernmental disclosure as a routine matter of coordinating law enforcement, so as to make it more effective. Tax returns should not be treated as a common resource for criminal investigations at all levels of government.

DISCLOSURE TO FOREIGN GOVERNMENTS

The Senate bills also authorize disclosure of information to foreign governments with whom the United States has mutual assistance treaties. Apart from the objection we noted to disclosure to state officials, which applies with equal or greater force to this provision, such disclosure is problematic for another reason. A nation with whom the United States has a mutual assistance treaty could seek access to taxpayer records for use in a criminal investigation for which the standards of proof are dissimilar from those in the United States. Moreover, what is a crime in a foreign country may not be criminal in the United States. The extraordinary coercive powers of the IRS should not be used to gain information about individuals which would then be used for purposes not only different from those for which the information was obtained, but also unsupported by any legitimate United States interest.

DISCLOSURE FOR "FOREIGN INTELLIGENCE" PURPOSES

Moreover, S. 1891 provides for dissemination of taxpayer information which is sought for use in "foreign intelligence collection or a foreign counterintelligence investigation." This is a particularly troublesome provision deserving the most serious scrutiny. Its overbreadth could potentially trigger a disclosure of tax information of citizens, including public officials, engaged in the most benign international activity. The chilling effect of such a provision on the exercise of free speech or the exchange of technological information could be devastating.

Such a vague and sweeping authorization for the invasion of taxpayer privacy is wholly unwarranted. The balance between the complementary interests of individual rights and crime control appears to be non-existent. What is the compelling justification for the proposal? What, if any, protections would taxpayer records have against fishing expeditions by FBI, CIA and other intelligence agencies seeking to utilize IRS as a general intelligence resource?

THE ASSISTANCE OF IRS IN JOINT TAX AND NONTAX INVESTIGATIONS

Both bills contain a new provision which states that: "No portion of this section shall be interpreted to preclude or prevent the Internal Revenue Service from assisting the Department of Justice or any other federal agency in joint tax and nontax investigations of criminal matters which may involve income tax violations [violations of this Title],[1] nor shall any portion of this section be interpreted to preclude or prevent the Internal Revenue Service from investigating or gathering relevant information concerning persons engaged in criminal activities which may involve income tax violations [violations of this Title].[1]

---

[1] S. 1891.

We find this section to be particularly problematic and confusing. An overbroad interpretation of its provisions could be used to negate all specific requirements of a court order to permit the disclosure or subsequent redissemination of taxpayer information by IRS to other federal agencies. There is no definition provided for what the term "assistance" means with in the context of joint tax and non-tax investigation by IRS and other federal agencies. The IRS is theoretically unbridled to provide a broad range of information without the "limitation" of judicial review.

The comment which accompanied submission of S. 732 indicates that "this section makes it clear on the face of the Statute that IRS is free to work jointly with other government agencies in combatting crime". This statement, of course, goes to the very heart of the issue embodied within these proposals. As we have shown previously, the IRS is not like other federal investigative agencies and should not be "free" to assist other agencies in carrying out functions, of government, for which it was not designed. Clearly, some further clarification of this provision is needed.

EXPEDITING PROCEDURES

We do support some of the proposed changes that would facilitate the process, provided adequate standards of privacy protection are met. We endorse the imposition of time limits; the extension to magistrates of the authority rule on government applications; and the provision allowing attorneys for the government, rather than heads of agencies, to apply for disclosure. In short, we endorse changes in the Tax Reform Act that will allow a constitutionally sound process, which respects individual rights, to proceed more expeditiously.

CONCLUSION

The claim that the proposed amendments put the IRS back into the fight against organized crime and drug traffic is a distortion. The IRS does not belong in that fight. Its special powers are not granted to facilitate law enforcement. To the extent that IRS in the past has been used as an investigative resource for other government agencies, its special authority was abused. The Tax Reform Act of 1976 was passed to correct those abuses. The current amendments threaten to undermine the Act by redefining the information that deserves protection, lowering the standard of proof necessary to justify disclosure and opening broader channels of dissemination. These changes carry with them an enormous potential for abuse and should not be adopted.

Moreover, the lack of empirical data to support sweeping changes in current law is especially notable. In light of the record of past abuses of taxpayer records, Congress has an affirmative duty to closely scrutinize any proposal that would erode constitutional protections. Congress must ask the difficult questions which lead to a clearer understanding of the nature of the problem to be solved. To assume the existence of a problem without a documented factual basis, and then to attribute the problem to current law, is the first step toward a return to an unbridled IRS. This approach has already proven to be violative of individual rights and the public interest.

There is a glaring need for documented information on the operation of the disclosure provisions under current law; perceptions alone are a wholly inadequate substitute for solid data. An analysis of the number and disposition of disclosure requests over a prescribed period may provide a useful basis for preliminary discussion. Thereafter, an analysis of the variables which affected negative disposition (including the training and familiarity of officials with existing procedures) may yield further insights. These questions are essential to any serious legislative inquiry into the operation of the Tax Reform Act.

Thank you for this opportunity to appear before the Subcommittee.

Chairman RANGEL. Thank you for your longstanding interests and your testimony.

To what extent would the ACLU provide guidelines as to whether and how the IRS could report evidence of illegal activities discovered from nonreturn information they have acquired? What should happen when IRS does find that very serious criminal activities are in fact taking place, and it is not related to the tax return at all, but is information that has been acquired in the course of a civil audit of the taxpayer?

Mr. **Shattuck**. I know that is a question concerning the subcommittee and it came out this morning in Senator Nunn's testimony.

Let me just repeat, we are absolutely opposed to imposing a requirement on IRS to conduct regular searches to determine whether there is any evidence that might relate to crime.

Now, that is what Senator Nunn's bill and the administration bill would do right now.

On a more reasonable basis, I think it might be possible to devise some approach which, let's say, identified the particular types of crimes, assume violent crimes, the hypothetical of a murder case was brought out this morning, and to provide that under circumstances where there is evidence that constitutes probable cause that the crimes of murder, airplane hijacking, rape or something amounting to that kind of a clear and immediate overwhelming violent crime evidence——

Chairman **Rangel**. What about plain old, ordinary, dirty, nonviolent crimes, like drug trafficking discovered during an audit of the returns of a dry cleaning establishment. The agent, in the course of checking it out—he is still an IRS agent—sees a wholesale drug distributing center. Nobody is being murdered and no planes are being hijacked.

Mr. **Shattuck**. The American Bar Association takes the position which we will look into ourselves, that current law does not prohibit the disclosure of that kind of information.

Chairman **Rangel**. I know that. I know that, but the agent does not want to make any problems.

I am just saying as one citizen to the other, how does he walk away from it and say, well, I am not required to make the disclosure. I am trying to find out, when he sees the drug transaction taking place and everybody else knows it is a regular plant, what does he do about it?

I know he can do anything he wants, but how far can you go in saying, clearly where a crime is being committed, that there is an obligation on that individual to disclose? Can you find anything that you would cite that the agent does not have to give up every file that he has for law enforcement in order to protect the privacy of the taxpayer?

Mr. **Shattuck**. No; really it is possible to imagine that there are circumstances under which that kind of probative evidence can and should be disclosed.

Chairman **Rangel**. We have a problem on the question of requirement.

We need your help there, because clearly when you mandate a requirement to report and the IRS agent now has to determine what is a crime and what is not a crime, we do have problems. But we have just as many problems where clearly in the course of a normal investigation, you stumble across something that is considered to be violative of every law of decency, as well as criminal statutes, then we have to do something. And even if you cannot necessarily support, because there are organizations that are created just to take moral positions, you can help us to try to change the law in such a way that we give the maximum protection to privacy and at the same time not look ridiculous when people are stumbling across dead bodies in the course of an audit.

Mr. **Shattuck**. The central problem is putting on the back of an IRS officer, an auditing official, what he or she might think is a general obligation to keep scratching their heads and wondering whether or not they have found evidence of crime. We do not want that officer to be put in the position of a more general investigative person, an FBI agent who is trained to look for evidence of that kind of crime, to have to make judgments that are unrelated to the enforcement of the tax code.

Chairman **Rangel**. I am certain that you do not have to do that, that the agency can say I haven't the slightest idea and refer it and let that other department or agency that has the training determine whether in fact a crime has been committed.

We cannot have the appearance that agencies are walking away from crime merely because of the rights of privacy. You do not want it, and I do not want it.

Thank you so much. We will be back in touch.

The committee would recess for 10 minutes and we would resume with our next witness from the General Accounting Office, Mr. Anderson.

Mr. **Shattuck**. Thank you, Mr. Chairman.

Chairman **Rangel**. Thank you.

[Recess.]

Chairman **Rangel**. The subcommittee will resume its hearing. We are anxious to hear from Mr. Anderson, Director of the General Government Division of the General Accounting Office.

STATEMENT OF WILLIAM J. ANDERSON, DIRECTOR, GENERAL GOVERNMENT DIVISION, GENERAL ACCOUNTING OFFICE, ACCOMPANIED BY JOHN GUNNER, EVALUATOR IN CHARGE, AND KENNETH MEAD, SENIOR ATTORNEY

Mr. **Anderson**. I would like to introduce the people at the table with me. To my left is Ken Mead, senior attorney, and to my right is John Gunner, an audit manager in our General Government Division, one who has done an awful lot of work in this area.

As I sat here and listened to the well-reasoned arguments pro and con on this legislation, I do not envy the subcommittee's task of trying to sort out right from wrong.

I would like to summarize my formal statement, sir, and add some highlights.

Chairman **Rangel**. Your full statement will appear in the record.

Mr. **Anderson**. First, there is now less coordination between IRS and the Department of Justice and other law enforcement agencies than existed prior to the Tax Reform Act of 1976. I think that was brought out clearly today.

Second, the effect on law enforcement of reduced access to tax information is difficult to gauge. Those in favor of changing the law hold that there are lost opportunities. There is anecdotal evidence to support this view but no clear picture of the overall situation.

Third, we are thus in the predicament of trying to weigh uncertain law enforcement gains against the equally uncertain extent to which some taxpayers' privacy would be reduced.

Having said that, though, let me state that GAO is in favor of changing the present law in some respects. We believe that the current emphasis on striking at the assets of drug and organized crime figures points up the desirability of some of the proposed changes.

I have testified in the past about how unsuccessful law enforcement officials have been in taking advantage of the asset forfeiture statutes. Tax information would ease their task somewhat, especially in view of the fact that in the past we have had little financial expertise available for use in this battle.

The FBI has had in the past a lot of accountant types, 1,200 by last count, but they really were not involved in asset forfeiture cases. That situation may be changing. Perhaps that is something to take into account in deciding how much we need to rely on the IRS and its financial expertise.

Our work has shown that the currently followed processes are absolutely discouraging attempts to obtain tax information. We have spoken to U.S. attorneys across the country and I will not read off the comments that they told us but generally they have been discouraged.

The point was made very effectively earlier in this hearing that some U.S. attorneys, though, are in fact making good use of the existing legislation to obtain tax information.

Chairman RANGEL. Who is discouraging the attorneys?

Mr. ANDERSON. The U.S. attorneys are discouraged by their perception that it is so complex and difficult to establish the probative nature of the tax information that they seek, that they even forego any attempts whatsoever. Twenty percent of U.S. attorneys have never even sought disclosure under current law.

Some figures that I have seen indicate that seven U.S. attorneys account for about 42 percent of all the requests that have been made under the current provisions.

Chairman RANGEL. Which proves that for some it is working?

Mr. ANDERSON. That is correct, sir, but there is room for considerable improvement in the guidance provided by the Department of Justice.

Chairman RANGEL. You are very kind in talking about the Justice Department's perceptions. You are saying they are inadequate and they do not use existing law?

Mr. ANDERSON. That is correct. There are untapped opportunities.

In addition, current law inhibits optimum use of information bearing on nontax criminal activities that IRS obtains in the course of its investigative efforts. We are persuaded that IRS does have some information like that.

What do we consider as the most important proposed changes?

First, the proposal that the criteria for court-ordered access to what I will call closely held tax information be changed to a showing of relevance rather than a showing of probativeness. I may have coined a new word there.

The point has been made that, well, the courts have been lenient in their interpretation of what represents probative evidence, but it is a fact that apparently they have not been in strict technical compliance with the requirements of the law, and if we accept that the access that has been obtained to date is reasonable, then we might as well make the law conform to current practice.

We have no qualms about reducing the level from probative to relevant.

Chairman RANGEL. Are you saying that the courts are interpreting the probative standard in a very liberal way?

Mr. ANDERSON. Yes. Now, there are two things to bear in mind. Nobody who has testified today mentioned any requests for court orders ever being declined. However, I think I have seen some statistics that we could produce for the record, that indicate there have been some declinations. There were about 450 requests for court orders approved through December 31, 1980. However, to date three requests have actually been declined by the courts.

It also must be recognized that there is a screening process within the Department of Justice, that would have taken out, I guess, would have stopped requests for court orders that were clearly not in conformity with criteria specified in the law, but the general understanding on the part of both the Department of Justice and IRS is that the courts have been liberal in granting these requests.

Chairman RANGEL. Thank you.

Mr. ANDERSON. Next there is a provision that would authorize IRS, no I am sorry, this is one that GAO would like to add that addresses a concern that you very properly raised earlier, that would authorize IRS subject to court approval, to release closely held tax information of interest in nontax criminal matters. In other words, you spoke of the problems about an IRS employee running across something that clearly indicated a nontax crime of some kind, and what does he do with the information.

Right now under existing law, if in fact the source of that information is not the taxpayer of a representative of the taxpayer, the IRS employee could refer the information to a disclosure specialist in IRS for a determination as to whether in fact it is releasable, and some figures that I have seen indicated that about half of the information referred to disclosure specialists is found to be releasable under the law and is sent forward to the Department of Justice.

We think that the same type of disclosure mechanism should be available for what I will call closely held tax information, but that IRS should be required in the case of closely held tax information to obtain an ex parte court order before releasing it.

Such a disclosure mechanism would afford a measure of privacy to the taxpayer, and would assure that in fact there is good cause to release the information outside of the IRS.

Chairman RANGEL. If I understand you correctly, in those matters that are not related to the tax form where in the agency's opinion there is in fact criminal activity, the agent could then go to the courts, reveal what information he has, and then a determination is made by the court as to whether or not that information is turned over to law enforcement?

Mr. ANDERSON. That is what we propose, sir, for the closely held type of information, yes.

Next we believe there is a need to redefine the categories of tax information. They are currently illogical, and I finally figured out what it was that bothered me about them yesterday.

First, we have the returns, the returns themselves. Then we have something called return information, and then parallel to that, we have something called taxpayer return information. Well, taxpayer return information is really a subdivision of return information which has two categories, taxpayer return information and other return information.

There is a problem applying these definitions that are currently in the law. I think we can understand why a lot of people have been confused about what is what, including even IRS people who are not certain as to where a particular piece of information lays in the various categories of tax information.

I would like to briefly cover now our views on the most important changes that need to be made to the proposed legislation.

We have some concerns about the changes that are proposed in H.R. 1502 and S. 732 and in the administration's proposal.

First, while agreeing with the concept of redefining categories of tax information, we disagree with the distinction that is drawn with respect to corporations, partnerships and other entities with three or more members.

We believe that the protections that are written into the legislation for individual taxpayers should apply to all tax return filing entities regardless of size. We agree with Mr. Shattuck that often there could be sensitive and privileged information included in the returns of large business entities, and it ought to be subject to the same tests of releasability as the information in returns of individuals and corporations and partnerships with two people or less.

Next, disclosure of nonreturn information. We believe that the authority to request access to such information should be limited to Department of Justice officials, and that that privilege should not extend to the heads of agencies and inspectors general.

A very practical reason for limiting this authority is to insure that the Department of Justice is well aware of all the criminal investigations that are going on across Government.

This past week I testified on the operations of the Inspector General at the Department of Health and Human Services. Specifically, on the cooperation and coordination between that organization and the FBI, and there are a lot of problems. Each is doing things that the other is not aware of, often affecting the very same cases. So one way to ameliorate a problem like that is to make sure that Justice is aware of all requests for tax information that are made.

Third, and I touched on this earlier, there is a need to authorize IRS to unilaterally disclose closely held tax information which pertains to non-tax Federal crimes, but such disclosure should be subject to IRS obtaining an ex parte court order.

Fourth, the emergency disclosure provision being proposed. We believe that it is subject to possible abuse as presently written. Emergency disclosure should be conditioned on a specific finding of IRS inability to obtain in a timely manner the ex parte court order that I just spoke about. In other words, the definition of emergency could be so loosely interpreted as presently written as to warrant unilateral disclosure by IRS in a wide range of circumstances without proper review by the judiciary.

Fifth, assistance of IRS in joint tax, nontax investigations. This provision seems much too broadly worded and it could be interpreted to perhaps override the rest of the proposed changes. We believe that some consideration should be given to sharpening the language there.

And finally, with respect to foreign intelligence access to tax information, we share some concerns that were voiced earlier. This provision is too broad, with access based only on the certification of the Attorney General. We believe that one possible corrective action that could be taken would be to, here again, require court approval for such disclosures. But as presently written, we think it is a little too broad.

That concludes my summary of the formal statement, sir, and we will try to respond to any questions you have

[The prepared statement follows:]

Statement of William J. Anderson, Director, General Government Division, U.S. General Accounting Office

Mr. Chairman and Members of the Subcommittee, we are pleased to be here today to discuss the issue of whether the existing tax disclosure statute strikes a proper balance between privacy rights and law enforcement information needs. Our testimony is based on extensive work we have done at various times over the last few years on the effects of disclosure restrictions on Federal law enforcement activities. This includes work we recently completed on behalf of this Subcommittee to evaluate the operation and effects of the disclosure statute. A detailed discussion of our objectives, scope, and methodology is included in appendix I.

Since its enactment, the disclosure section of the 1976 Tax Reform Act has generated much concern and controversy because it has affected coordination between IRS and law enforcement agencies. We recognize that changes to the disclosure statute will not suffice to solve all of the problems Federal agencies encounter in seeking to bring criminals, such as narcotics traffickers, to justice. However, changes to the statute would constitute an important step toward resolving coordination problems. We also recognize that, in considering changes to the law, it is essential to strike a proper balance between legitimate privacy concerns and equally legitimate law enforcement information needs.

In this regard, our work in the disclosure area has been guided by two basic principles. First, the Internal Revenue Service (IRS) is not primarily a criminal law enforcement agency. Rather, its primary mission is to collect taxes and to encourage and achieve the highest possible degree of voluntary compliance with the tax laws. Second, taxpayers who supply information to IRS have a basic right to privacy with respect to that information. Such information should be subject to disclosure for nontax purposes only when society has a compelling interest which outweighs individual privacy concerns.

With these principles in mind, I would now like to discuss the (1) purpose of section 6103 of the Internal Revenue Code, the tax disclosure statute, (2) effects of section 6103 on IRS and other law enforcement agencies, and (3) changes that can be made to the existing statute to help resolve coordination problems while still protecting taxpayers' privacy rights.

CONGRESS ENACTED THE DISCLOSURE STATUTE TO SAFEGUARD TAXPAYERS' PRIVACY RIGHTS AND TO PREVENT ABUSES

IRS probably has more information about more people than any other government agency in this country. Consequently, agencies needing information about people have sought to obtain it from IRS. Before the enactment of the Tax Reform Act of 1976, procedures for disclosing tax information had developed in a piecemeal manner. Various statutes, regulations, and executive orders were promulgated without sufficient consideration of a comprehensive approach to the disclosure of such information.

Concern over the uses being made of tax information manifested itself in 1973 after the President issued Executive Order 11697, authorizing the Department of

Agriculture to inspect the tax returns of all farmers "for statistical purposes." Following the issuance of that order, two subcommittees of the House of Representatives held hearings on the department of Agriculture's need for such access to tax data. During those hearings, strong sentiments against the order were voiced and Department of Justice officials expressed concern that the order would be a prototype for future orders which would open more tax returns to inspection by other agencies. Responding to the adverse sentiment expressed in the two hearings, the President revoked the order on March 21, 1974.

Concern over tax return confidentiality surfaced again in 1974 during hearings by the Senate Select Committee on Presidential Campaign Activities (Watergate Committee) and the House Judiciary Committee investigating the possible impeachment of the President. The Senate Committee's hearings revealed that the White House had sought and obtained tax information from IRS, including political information concerning individuals included on the so-called "enemies list." One of the Articles of Impeachment proposed by the House Committee alleged that the President had endeavored to obtain from IRS, in violation of the constitutional rights of citizens, confidential information contained in income tax returns for purposes not authorized by law.

Congressional interest in tax return confidentiality was futher underscored when the Congress enacted the Privacy Act of 1974. Among other things, that act established an independent Privacy Protection Study Commission and required it to report to the President and the Congress on whether IRS should be prohibited from transferring individually identifiable data to other Federal agencies and to agencies of State governments.

After conducting public hearings and reviewing policies, procedures, and practices regarding Federal tax return confidentiality, the Commission issued a report to the President and to the Congress in June 1976 with the following recommendations:

IRS should be prohibited from disclosing individually identifiable data unless specifically authorized by the concerned individual or by Federal statute.

Congress should specify by statute the categories of tax information IRS can disclose and the purposes for which disclosure can be made.

IRS should be prohibited from disclosing any more individually identifiable taxpayer information than is necessary to accomplish the purpose for which the disclosure has been authorized.

Recipients of tax information should be prohibited from redisclosing it without the concerned taxpayer's consent or specific statutory authorization.

In developing its recommendations, the Commission sought to take into account the relationship between tax return confidentiality and voluntary compliance. While noting that no one had sought to measure that relationship, the Commission stated its belief that the effectiveness of our Nation's tax system depends on the confidentiality of tax returns and related information. It further stated the belief that widespread use of tax information for non-tax purposes could not help but diminish taxpayers' desire to cooperate with IRS.

The Congress considered the Commission's recommendations, extensively debated the issues, and with the record of alleged and actual abuses of tax information still fresh in mind, enacted the Tax Reform Act of 1976. The disclosure section of that act, which became effective on January 1, 1977, set forth all of the permissible uses of tax information and specifically prohibited all other uses.

THE DISCLOSURE STATUTE HAS REDUCED COORDINATION BETWEEN IRS AND OTHER LAW ENFORCEMENT AGENCIES AND NEEDS TO BE AMENDED

In enacting the disclosure statute, the Congress clearly signaled its intent that IRS should concern itself primarily with its basic mission—encouraging and achieving the highest possible degree of voluntary compliance with the tax laws. On the other hand, the Congress did not intend to put a halt to appropriate use of tax information in non-tax criminal investigations and prosecutions. Rather, it sought to place tight controls on uses of that information in an effort to prevent infringements on taxpayers' privacy rights. Unfortunately, however, the disclosure statute has adversely affected cooperation and coordination between IRS and other law enforcement agencies in four major ways. Specifically, since the statute's enactment,

IRS' ability to coordinate effectively with Justice Department attorneys and other law enforcement agencies has been reduced;

Justice attorneys and other law enforcement officials have been discouraged from seeking tax information to the point that little use has been made of such information for non-tax criminal investigative and prosecutive purposes;

IRS has been precluded from informing law enforcement officials about certain information it possesses concerning non-tax crimes, even under emergency circumstances; and

Justice attorneys have been prevented from using certain tax information, obtained during criminal investigations, in related non-tax civil proceedings.

I would now like to discuss each of these four problems in some detail.

IRS cannot effectively coordinate its investigations with the Justice Department and other law enforcement agencies

Coordination between IRS and the Department of Justice is essential to efficient Federal law enforcement. U.S. attorneys, for example, are responsible for prosecuting individuals charged with Federal violations, including criminal tax violations. To effectively carry out their responsibilities, U.S. attorneys have to be aware of the investigative efforts of numerous agencies. This enables the attorneys to coordinate Federal law enforcement efforts, help prevent duplicative investigations, provide investigative guidance, and otherwise assist Federal law enforcement officials in developing successful cases. Likewise, Strike Force attorneys are responsible for coordinating the efforts of various Federal law enforcement agencies against organized crime.

Under the disclosure statute, however, U.S. attorneys and Strike Force attorneys often cannot coordinate IRS' criminal tax investigations with the non-tax investigations conducted by other Federal agencies. This is because the disclosure statute, as interpreted by IRS, generally prohibits the Service from discussing the specifics of contemplated or ongoing investigations with Justice attorneys. Such discussions cannot take place until the cases are referred to Justice for prosecution. Thus, because Justice attorneys often do not know the identity of taxpayers under investigation by IRS for possible criminal violations of the tax laws, they cannot fully carry out their prescribed duties.

Documenting the frequency and severity of coordination problems is a difficult, and sometimes impossible, task. One would very much like to know how many investigations and prosecutions were foregone for lack of tax information. But, such empirical data cannot be gathered because investigators and prosecutors cannot specify what would have resulted from work they never initiated or never carried to a consclusion. Even so, there is sufficient information available in the form of specific examples, limited statistics, and statements from IRS and law enforcement officials to confirm that coordination problems exist.

IRS, for example, has been able to provide some statistics and specific case examples where inability to coordinate with Justice attorneys has resulted in unsuccessful criminal tax cases. In this regard, Justice attorneys have prosecuted individuals on non-tax criminal charges without knowing about ongoing tax investigations of the same individuals. In such instances, the attorneys lose the added advantage that the tax violations might have brought to their cases. In addition, prosecutions on non-tax charges can render IRS investigations meaningless because Justice's "dual" and "successive" prosecution policies generally require that all offenses arising from a single transaction, such as narcotics trafficking and evading taxes on the ensuing profits, be tried together. Those policies recognize the difficulties a Justice attorney would face in seeking to secure a second conviction on the basis of essentially the same set of facts. This is not to say, however, that Justice would not consider the feasibility of bringing a second prosecution on separate charges in cases where the initial prosecution results in an acquittal.

In fiscal years 1976 through 1981, IRS discontinued 507 criminal tax investigations because the investigative targets were being prosecuted by another agency or had been incarcerated. Another 185 completed investigations did not result in prosecutions on criminal tax charges for the same reasons. If IRS had the authority to discuss specific investigative targets with Justice attorneys, some of these cases could have resulted in prosecutions on tax charges in lieu of other charges, or multiplecount prosecutions composed of both tax and non-tax criminal charges. In addition, if Justice attorneys deemed the non-tax charges more viable, IRS could have saved resources by discontinuing some cases at an earlier date. The following examples illustrate the problems.

An individual who had failed to report at least $150,000 during a 2-year period was sentenced to 1 year in prison on a narcotics misdemeanor. IRS attorneys did not forward the criminal tax case to Justice for review because the individual already had been incarcerated. If IRS had been able to discuss its ongoing investigation with Justice, the affected attorney could have considered bringing a prosecution on tax and/or narcotics charges. Instead, IRS' criminal case was rendered meaningless.

In another case, the Department of Justice declined to prosecute a Drug Enforcement Administration class I narcotics violator on criminal tax charges because he pled guilty to a felony indicitment count carrying a maximum sentence of 5 years in prison. Subsequently, the individual was sentenced to 5 years probation. IRS' investigation thus proved useless from a criminal tax standpoint. If IRS had been able to discuss this case with Justice during its early investigative stages, the Service would have quickly determined that its case had little prosecutive potential. Accordingly, the criminal tax investigation could have been immediately discontinued, thus saving IRS resources.

The disclosure statute also appears to be responsible in part for a decline in IRS' participation in strike force cases and a recent increase in reliance on the grand jury investigative process. At the end of fiscal year 1976, IRS had 616 strike force cases in inventory. The disclosure statute was signed into law in October 1976 and became effective on January 1, 1977. According to Justice and IRS officials, their resulting inability to discuss potential targets and ongoing investigations resulted in a decline in IRS' participation in the program. By the end of fiscal year 1977, IRS' inventory of strike force cases had declined by 46 percent to 335 cases. Significantly, IRS' strike force case inventory has never since approached pre-1977 levels. For example, at the end of fiscal year 1981, IRS had 316 active strike force cases.

Although IRS' inventory of strike force cases has declined, its involvement in grand jury cases has increased significantly. Soon after enactment of the disclosure statute, Justice attorneys apparently decided that the most effective way to coordinate with IRS special agents throughout an investigation was to get one or more IRS employees assigned as agents of a grand jury. As a grand jury agent, an IRS employee may develop tax information and discuss applicable cases with the responsible Justice attorney. Thus, problems with front-end and continuing coordination largely are resolved under this investigative approach.

Despite the utility of the grand jury investigative process as it relates to coordination and cooperation with IRS, Justice attorneys did not begin making extensive use of it until recently. This is because Justice attorneys had to content with a time-consuming, multi-tiered IRS/Justice administrative review process in order to get approval for IRS participation in a grand jury investigation. This matter was explored in hearings before the Senate Subcommittee on Treasury, Postal Service, and General Government in April 1980.

In June 1980, IRS streamlined the grand jury approval process by eliminating some levels of review and placing time limits on others. Subsequently, its inventory of grand jury cases climbed by 62 percent, from 765 in September 1980 to 1,233 in August 1981. Of those 1,233 cases, 1,080, or 88 percent, were directed at individuals who derive their income from illegal activities. Moreover, of the 316 strike force cases in IRS' inventory at the close of fiscal year 1981, 247, or 78 percent, were being carried out through the grand jury investigative process; few strike force investigations were being carried out under IRS' normal administrative processes. Although comparable statistics for prior years were unavailable, the Director of IRS' Criminal Investigation Division told us that relatively few cases were carried out under grand jury auspices in the past.

Thus, the disclosure statute may have inadvertently encouraged use of the grand jury investigative process—a process under which disclosure of certain information by witnesses is cumpulsory—and reduced reliance on the normal administrative process for investigations. This is not to say that the grand jury process is being abused. We have no way of knowing the extent to which disclosure problems enter into decisions to establish a grand jury because we do not have access to grand jury case files. Moreover, increased use of the grand jury process also is attributable to recent changes in IRS policies which encourage joint investigations with other agencies. Further, prosecutors seem to have become more sophisticated in recent years in terms of the types of crimes they investigate and the techniques they use in carrying out investigations. And, the grand jury process is a key investigative technique. Still, on the basis of limited discussions with IRS and Justice officials, it is apparent that disclosure restrictions also enter into the grand jury decision process in some fashion.

Finally, our discussions with IRS, the Drug Enforcement Administration (DEA), and U.S Customs Service officials, both at headquarters and in the field, further illustrate some of the problems these agencies face in terms of coordinating their investigations. Customs officials stated that, with the exception of a few key projects, they generally do not seek to coordinate their investigations with IRS due to the disclosure statute. IRS and DEA officials cited various disclosure-related problems they have encountered in actively seeking to coordinate their investigative efforts. For example, DEA routinely provides IRS with names and background information on high level drug traffickers. If IRS decides to initiate a tax investigation of a DEA target, it cannot inform DEA because of the disclosure statute. However, IRS can legally seek further information about the specific individual from DEA. By doing so, IRS presumably alerts DEA to the existence of its investigation. DEA can then seek court-ordered disclosure of tax information on the individual or may file a written request for tax information. Through this "routine," DEA and IRS sometimes learn that the agencies are conducting concurrent investigations. However, there is no guarantee that DEA will pick up the "signal" in such instances; nor is there any guarantee that DEA will have sufficient information on which to base a court order or written request. Thus, current law does not insure effective coordination in every instance.

IRS has at times detailed some special agents to work as consultants to DEA Central Tactical teams. The IRS agent's role under such conditions involves helping DEA analyze financial information. Because of the disclosure statute, however, the agent has no access to tax information.

IRS special agents often are given access to DEA files for the purpose of looking for leads. If IRS follows up on any leads it identifies, the aforementioned "routine" may ensue and effective coordination may or may not result.

In a few cities, IRS agents have been assigned to DEA offices for two purposes. First, they function as consultants to DEA but have no access to tax returns or tax information. Second, they can feed leads to IRS but cannot work the leads as IRS cases. Instead, other IRS agents, not assigned to DEA, work the leads but in doing so they cannot discuss the cases with the IRS agents working with DEA. Thus, there is no direct communication between DEA and the IRS investigator who has access to tax information.

Clearly, DEA and IRS have sought to establish coordination mechanisms to the extent feasible under existing law. These efforts were prompted in part by congressional oversight activities. Still, despite the agencies' efforts, problems persist. In the final analysis, the agencies cannot directly coordinate their activities. And, as previously discussed, Justice attorneys have been unable to fill the coordination gap for the two agencies due to disclosure restrictions.

In sum, the disclosure statute prevents IRS from efficiently and effectively coordinating its efforts with Justice attorneys and other law enforcement agencies. Clearly, if IRS is to become a full partner in Federal efforts to combat crime, legislative changes are needed.

Existing mechanisms for obtaining access to tax information are not used extensively

The second adverse effect of the disclosure law is that little use has been made of tax information for non-tax criminal investigative and prosecutive purposes.

In this regard, certain Federal agencies have a bonafide need for tax information in pursuing non-tax criminal investigations and prosecutions. The Congress recognized this need and authorized two means through which Federal agencies, such as the Justice Department, could gain access to tax information. To obtain information supplied to IRS by a taxpayer, an agency head must obtain a court order. To obtain information supplied to IRS by third parties, an agency head must file a written request for the information with IRS.

Since January 1977, we have monitored the utility of these two access mechanisms. The Congress thought that U.S. attorneys and Strike Force attorneys would be the prime users of tax information for non-tax criminal purposes. From the outset, however, the attorneys perceived that it would be difficult to meet the criteria to obtain a court order and that the administrative process would be burdensome and time-consuming. As a result, many Justice attorneys decided that they would carry out their duties as well as they could without tax information.

When the disclosure law became effective, both IRS and Justice centralized their controls over the two authorized access mechanisms, requiring that requests for tax information be channeled through their respective headquarters offices. IRS' decision to centralize its controls stemmed from concern that the complexity of the law would cause confusion and result in criminal and civil court actions against employees for unauthorized disclosures. Justice, on the other hand, had no choice but to centralize its controls because the authority to request tax information is vested by law with only a few top-level agency officials.

Centralization of controls by IRS and Justice confirmed the perceptions of many Justice attorneys. To obtain a court order, the attorneys not only had to meet certain stiff legal tests but had to deal with a burdensome administrative process as well. The process required an attorney to get Justice headquarters approval for seeking a court order; to obtain the court's approval for the order; and to sent the order, if obtained, to IRS headquarters. Then, the attorney had to wait while IRS (1) sent the order to its appropriate field office, (2) gathered the requested information in the field office, (3) reviewed the information gathered, and (4) transmitted the information to Justice. A similar, if only slightly less burdensome, process had to be followed to obtain third-party information from IRS.

As a result, requests for tax information declined precipitously. Justice reported, for example, that its attorneys had made 1,816 requests for tax information in 1975. In contrast, IRS statistics indicate that, on average, Justice attorneys made 274 requests annually during calendar years 1977 through 1980—the first 4 years the disclosure statute was in effect.

Then, in March 1980, the Department of Justice completed a survey of the views of Departmental personnel on the utility and workability of the access mechanisms. The survey results indicated that Justice attorneys considered the mechanisms too cumbersome and time-consuming to justify usage. Our discussions with Justice attorneys in March and April 1980 confirmed the results of the survey. We also determined, however, that the disclosure process could be streamlined under existing law. Accordingly, in testimony before the Subcommittee on Treasury, Postal Service, and General Government, Senate Committee on Appropriations, in April 1980, we recommended that IRS decentralize its disclosure process. Such action seemed feasible because, by that time, IRS had given its employees disclosure training and had assigned one or more disclosure specialists to each IRS field office. IRS implemented our recommendation in June 1980.

Justice, in consultation with IRS, then prepared and issued supplemental disclosure guidance for use by U.S. attorneys and Strike Force attorneys. The guidance proved particularly valuable in that it formalized an advance notification process. Under that process, Justice attorneys alert IRS to the fact that they plan to seek a court order or obtain a written request for tax information from Justice headquarters. IRS then can immediately begin trying to locate the needed information, although the information cannot be supplied to Justice until IRS actually receives a validated order or request.

In response to this Subcommittee's request, we recently sought to determine whether the cited administrative changes had achieved the desired effects. We found that the disclosure process had in fact become more timely and less burdensome.

In this regard, we obtained information on all court orders and written requests filed with five IRS district offices—Boston, Dallas, Jacksonville, Los Angeles, and Manhattan—during June 1, 1980, through September 30, 1981. The Boston district had received 9 requests and processed them in an average of 47 calendar days. In Dallas, 3 requests were processed in an average of 33 days. Jacksonville needed 20 days on average to process 28 requests, while Los Angeles averaged 37 days in processing 15 requests. In Manhattan, 22 requests were processed in an average of 29 calendar days. In contrast, prior to decentralization, 4 IRS district offices we visited early in calendar year 1980—Jacksonville, Los Angeles, Manhattan, and Philadelphia—needed from 50 to 80 days, on average, to process court-ordered disclosures, and from 68 to 88 days, on average, to process written requests.

Justice headquarters officials informed us that, despite the aforementioned administrative efforts to streamline the disclosure processes under current law, attorneys still are not making as much use of the access mechanisms as they could. The officials cited two reasons for this. First, attorneys perceive that it is difficult to meet the criteria the law sets forth for approvals of court orders and written requests. Specifically, before obtaining a tax return, an attorney must demonstrate that it is "probative" and that the information cannot reasonably be obtained from another source. With respect to written requests, an attorney must specify why the third-party information is "material" to an investigation. These are perceived as "catch 22" situations. Second, the attorneys perceive both the court-ordered and written request disclosure processes to be time-consuming and overly burdensome.

Our discussions with U.S. attorneys in Boston, Dallas, Jacksonville, Los Angeles, and Manhattan supported the validity of the headquarters' officials statements. In general, the attorneys informed us that, despite the administrative efforts made to streamline the processes, they still consider existing disclosure mechanisms to be time-consuming, burdensome, and otherwise unworkable. The attorneys stated that tax information can be of great value for investigative and prosecutive purposes in a variety of cases but that problems with existing access mechanisms prevent them from getting needed tax information in all but a few cases. The attorneys further stated that the disclosure statute has seriously impaired coordination between Justice and IRS.

For example, the U.S. attorney in Manhattan told us that his office's relationship with IRS is poor, primarily because of the cumbersome and time-consuming processes associated with the disclosure statute in Justice and IRS. In Boston, the U.S. attorney told us that coordination with IRS simply does not take place except through the grand jury investigative process. He further stated that his office generally seeks to develop cases without using IRS and does not pursue many cases which require tax information for successful prosecution.

Likewise, the U.S. attorney in Jacksonville stated that he has very little contact with IRS as a result of the disclosure restrictions. In Los Angeles, an assistant U.S. attorney, noted for his financial investigative expertise, told us that he has an excellent working relationship with IRS, primarily because he relies on the grand jury investigative process. He said he had long ago decided not to rely on the cumbersome, time-consuming access mechanisms authorized under the disclosure statute. The U.S. attorney in Dallas told us that he has a good relationship with IRS despite the fact that it takes about a month to get tax information under existing procedures.

We also discussed these issues with Strike Force attorneys in Boston, Kansas City, Los Angeles, Miami, and New York. The attorneys consistently described existing access mechanisms as cumbersome, time-comsuming, and otherwise unworkable. These attorneys indicated that they had made few or no requests for tax information, preferring instead to rely on the grand jury investigative process.

Besides problems with Justice attorneys' perceptions regarding the utility of existing access mechanisms, the utility of the mechanisms has been limited by misunderstandings and differences over legal interpretations. Perhaps the best examples of such problems can be found in debates and discussions over the meanings of section 6103 definitions of a "return," "return information," and "taxpayer return information." For example, agencies have filed written requests for tax information with IRS and subsequently been advised that the information they seek can be released only via court order. In this regard, only "return information" can be disclosed via written request. A "return" and/or "taxpayer return information" can be disclosed only via court order. In such instances, IRS is merely complying with the law. Unfortunately, under such circumstances, requesting agencies tend to perceive that getting information from IRS is a difficult task.

The complex definitions contained in current law constitute the underlying cause of many of the problems encountered by IRS and other agencies. In fact, many of the extreme case examples of coordination problems, cited in various congressional hearings, stem from misunderstandings or differences over legal interpretations of the definitions. In one such instance, IRS classified the contents of a taxpayer's trash can as taxpayer return information and refused to turn over the information it had gathered without a court order. The Department of Justice did not agree with IRS' interpretation in this particular instance.

Despite all of these problems, some Justice attorneys have been successful in obtaining needed tax information from IRS under current procedures. For example, during calendar years 1977 through 1980, Justice attorneys sought and obtained 447 court-ordered disclosures—an average of about one approved order per U.S. attorney and Strike Force attorney per year. Similarly, the attorneys sought and obtained IRS approval of written requests 600 times during the same 4-year period—an average of about 1.3 such requests per attorney per year.

These statistics, however, are subject to varying interpretation. Proponents of current law, for example, could cite these statistics as evidence that existing access mechanisms would be viable but for the lack of a good faith effort on the part of Justice attorneys. On the other hand, proponents of revisions to current law could point out that the statistics measure only those cases which reached the courts and IRS, but ignore instances in which tax information was not sought when needed due to difficulties in meeting the criteria, excessive administrative burden, or lack of timeliness in disclosure processes.

In our view, each argument has merit. On the one hand, it seems clear that Justice attorneys could have obtained access to more tax information in past years had they sought to work more effectively within the constraints of current law. On the other hand, it is also clear that Justice and IRS have sought to facilitate administrative processes under current law and succeeded in some respects. Nevertheless, Justice attorneys still seem reluctant to seek access to tax information due to a variety of problems with current law.

In this regard, the five U.S. attorney offices we recently visited had sought tax information, via court order or written request, only 58 times during the 16-month period ending September 30, 1981. Significantly, this was the time period during which IRS' decentralized disclosure process was in effect and Justice attorneys were operating under the supplemental guidance afforded them by the Department. Thus, despite the administrative changes, the attorneys still perceived that it would be difficult to meet certain criteria and that existing processes are time-consuming, burdensome, and otherwise unworkable. Those are the reasons they cited for not seeking access to tax information in numerous other instances in which tax data could have been of value to them from an investigative or prosecutive standpoint.

Given all of the above, we see a need for several legislative changes, as well as an administrative action. Some relatively minor revisions to the law can make certain criteria more reasonable and improve timeliness. However, it will also be necessary for Justice to further encourage its attorneys to work within the disclosure constraints which still will exist. The Attorney General can do so by issuing a directive on this matter to affected Department personnel and by subsequently monitoring Department compliance with his directive.

IRS cannot disclose certain information about non-tax crimes, even under emergency circumstances

A third adverse effect of the disclosure statute relates to IRS' authority to release information concerning non-tax crimes.

In conducting their daily activities, IRS employees sometimes obtain information indicating that a particular taxpayer has committed a crime outside IRS' jurisdiction. If such information is obtained by IRS from a third party, IRS can take the initiative in disclosing the information to the head of the appropriate Federal agency including the Attorney General. However, if that information is obtained from a taxpayer, his records, or his representative, IRS cannot legally alert the Attorney General or other Federal agency head regardless of the crime's seriousness. Furthermore, the disclosure statute generally prohibits IRS from revealing any evidence of non-tax violations to State and local authorities regardless of whether the information is obtained from the taxpayer or from a third party.

The following are examples of situations in which IRS was able to disclose information because it was obtained from a a third party and involved a Federal crime.

A special agent received a telephone call from an unidentified informant who alleged that a particular employee of another Federal law enforcement agency was providing advance information on bookmaking enforcement operations to a criminal who might have been affected by such operations.

While reviewing and discussing a third party's records as part of a criminal tax investigation, a special agent was informed by that individual that the taxpayer's ongoing trial for fruadulent loan practices would result in an acquittal because a "deal" had been made with the judge.

During a criminal tax investigation, a witness told a special agent that the subject taxpayer had stated that a particular United States Customs agent would assist in smuggling drugs into the country.

In contrast, IRS was unable to notify Justice of the following situations because the information was obtained from the subject taxpayer, his return, or his representative.

A taxpayer blatantly listed "narcotics" as his occupation on his tax return and, over a 2-year period, reported well over $200,000 in revenues for the "sale of controlled substances." Because the information was reported on a tax return, IRS could not refer the matter to the Justice Department.

Books and records provided by a taxpayer to a revenue agent during an examination indicated that the taxpayer was involved in check kiting, with several million dollars of fictitious deposits made to 7 banks over a 1-year period. This information could be be disclosed to the Justice Department because it had been provided by the taxpayer.

During an interview with an IRS special agent, a taxpayer revealed having made kickbacks to a government official in return for the award of certain contracts. The public official's alleged misconduct could not be reported to Justice by IRS because it was obtained from the taxpayer who shared involvement.

A secretary employed by a corporation which was being audited by IRS alleged to the revenue agent that the corporation's president had disposed of some firearms in a manner which violated the law. Because she was acting as a representative of the taxpayer at the time of the allegation, the information could not be passed on to the Justice Department.

These examples illustrate situations in which IRS is precluded from turning over non-tax criminal information to Justice. The rules governing such disclosures apply regardless or the seriousness of an offense, the type of law violated, or whether emergency circumstances are involved. Thus, the statute as presently written would preclude IRS from disclosing information obtained from a taxpayer, or his or her representative, even if it related to the passing of national security information to a foreign country for a fee, the potential assassination of a public official, or a State criminal offense, like murder.

We find it difficult to justify the cited restriction on IRS' authority to disclose information concerning non-tax crimes. In our view, the law needs to be amended to remedy this situation.

Justice attorneys cannot use certain tax information in related civil proceedings

A fourth adverse effect of the disclosure statute relates to the use of tax information in civil proceedings arising from a criminal investigation.

Current law authorizes Justice attorneys, through court order or written request, to obtain tax information for use in non-tax criminal cases. However, information the attorneys obtain from IRS through these processes cannot be used in civil proceedings directly related to the criminal investigation.

For example, under Title 21, Section 881 of the U.S. Code, Justice attorneys may seek civil forfeiture of vehicles, equipment, and other items used to facilitate narcotics transactions. In addition, since November 1978, this statute also provides for civil forfeiture of money or other property used in exchange for a controlled substance. In some instances, a Justice attorney investigating a drug trafficker for criminal violations will seek tax information from IRS. If, however, the attorney subsequently decides to concurrently pursue the trafficker under Section 881, he cannot use the tax information obtained from IRS as part of the civil case.

This is but one example of a situation in which tax information, obtained legitimately be a Justice attorney for criminal prosecutive purposes, may not be used in a related civil proceeding. Similar situations can arise under the civil rights, antitrust, fraud, and organized crime statutes. In our view, the disclosure statute needs to be amended to permit use of tax information under such circumstances.

NEED FOR REVISIONS TO THE DISCLOSURE STATUTE

After almost 5 years of experience with the disclosure provisions, it is apparent that coordination and cooperation between IRS and law enforcement agencies have been adversely affected. While some administrative actions have been taken to enhance law enforcement efforts, legislative changes also are needed. However, there is no need to completely revamp existing law; instead, refinements can be made to resolve coordination problems while still protecting important privacy rights. Specifically, we suggest the following:

Clear tax information categories are needed. The manner in which tax information is categorized and defined is extremely important because the law affords various levels of protection to different kinds of information. Present law defines and affords certain levels of protection to a "return," "return information," and "taxpayer return information." However, as experience with the Tax Reform Act demonstrates, these definitions have proven confusing to IRS employees, Justice Department officials, and other Federal agencies. Thus, existing categories and definitions of tax information need to be simplified. This can be accomplished without changing the levels of protection presently afforded to the various categories of tax information.

The authority to seek access to tax information, via court order or written request, needs to be extended to U.S. attorneys and Strike Force attorneys. Currently, these attorneys must obtain the written approval of an assistant attorney general in every instance in which they seek access to tax information. Decentralizing authority to the attorneys themselves would improve the timeliness of the existing disclosure process and help alter the negative perceptions Federal prosecutors now have of the current system.

The criteria that Justice attorneys must meet to obtain a court order should be amended. Presently, attorneys must show, based on reliable information, that there is reasonable cause to believe a crime has been committed and there is reason to believe that the information sought from IRS is probative. Under a strict interpretation of the law, this creates a "catch 22" situation—attorneys must show that tax information, which they haven't yet seen, constitutes probative evidence that a crime has been committed. A less burdensome standard could be substituted without jeopardizing taxpayers' rights.

IRS needs to be authorized, with accompanying safeguards, to disclose information concerning non-tax crimes it obtains from taxpayers while carrying out its normal tax administration functions. To prevent abuse, we recommend that such disclosure to subject to advance approval by a court.

Likewise, IRS needs to be authorized to disclose certain information concerning non-tax crimes under emergency circumstances. These circumstances could be defined in part and controlled by keying such an authorization to IRS' inability to timely obtain court approval before making the disclosure.

Justice attorneys need authority to use tax information, which has been properly obtained for use in non-tax criminal proceedings, in related civil proceedings. Increasingly, prosecutors have recognized the utility of financial investigations and forfeitures as weapons against criminals. Tax information can be very useful to prosecutors who seek both criminal and civil action against suspects.

IRS needs to be authorized to discuss ongoing criminal tax investigations with Justice, as necessary, prior to formally referring the cases to Justice for prosecution. Under current law, as interpreted by IRS, front-end and continuing coordination of tax investigations is generally prohibited. This prevents Justice attorneys from fully carrying out their prescribed duties and can cause significant inefficiencies. It has affected IRS participation in strike force activities and may have promoted use of the grand jury investigative process. Further, it has limited coordination between IRS and other law enforcement agencies. At a minimum, there is a need for the Congress to clarify its intent as to whether IRS can coordinate ongoing investigations with Justice.

Problems with the current disclosure statute have been discussed and debated in extensive hearings before various subcommittees. In December 1979, the Senate Permanent Subcommittee on Investigations explored these disclosure issues in detail, through 5 days of hearings. As a direct result of those hearings, several Senators jointly sponsored a bill—S. 2402—which, if enacted, would have substantially revised the disclosure statute.

We analyzed S. 2402 in detail and issued a report (GGD-80-76, June 17, 1980) recommending a series of revisions to the proposed bill. We also testified on S. 2402 before the Senate Finance Subcommittee on Oversight of the Internal Revenue Service on June 20, 1980. Many of our suggestions were adopted in a revised version of the bill—S. 732—which was introduced in the Senate this year. The same bill was introduced in the House this year as H.R. 1502.

H.R. 1502 would resolve many of the problems discussed earlier in my statement. However, it needs further modification to strike a better balance between privacy concerns and law enforcement information needs. Appendix II to my statement discusses our suggested modifications in detail and provides suggested * * *.

Recently, the Administration proposed a bill to revise the disclosure statute. It was recently introduced in the Senate as S. 1891. The proposal closely tracks H.R. 1502 although it does contain some differences. Like H.R. 1502, the Administration's proposal needs further refinement. The legal analysis contained in appendix II also specifies our views on how that proposal ought to be modified.

In summary, the disclosure statute has afforded taxpayers increased privacy over information they provide IRS. It has also affected coordination between IRS and other agencies and thus has had an adverse effect on law enforcement efforts. The extent of that effect is difficult to measure and, in fact, may not be measurable. However, one fact is clear—despite administrative actions aimed at facilitating coordination and cooperation under existing law, problems persist. Thus, to help improve the effectiveness of Federal law enforcement efforts, legislative changes are needed to facilitate cooperation between IRS and other agencies. The Congress could accommodate this need and still maintain essential privacy controls by enacting a modified version of either H.R. 1502 or the Administration's proposal.

THE DISCLOSURE STATUTE LIMITS GAO'S ABILITY TO CARRY OUT ITS CONGRESSIONALLY MANDATED RESPONSIBILITIES

Mr. Chairman, we would also like to briefly discuss problems we have encountered with the disclosure statute while seeking to fulfill our congressionally mandated responsibilities.

Although our authority for gaining access to tax data for purposes of evaluating tax administration activities is generallly sufficient, we have insufficient access authority with respect to non-tax administration Government activities. Specifically, we have experienced access-to-records problems when seeking tax return information to evaluate and assess certain Federal programs involving retirement, disability, food stamps, housing, and welfare.

For example, earnings information permeates Social Security Administration files and IRS considers that data to be tax return information. As a result, we almost had to stop our evaluations of Social Security Administration operations. So that we could continue our work, the Chairman of the House Ways and Means Committee designated us an agent of the Committee. In designating GAO as the Committee's agent, the Chairman recognized the detrimental impact of IRS' interpretation on our ability to assist the Congress, extended our access to other non-tax administration agencies, and stated that "this is intended to be a temporary resolution of GAO's status under the Code's disclosure provision until a legislative solution can be effected."

Although that arrangement temporarily solved the immediate problem, we agree with the Chairman that it is not a satisfactory permanent solution. A temporary authorization does not provide GAO with the continuous access it needs to effectively carry out its role and responsibilities. Without such access, we lack a sufficient basis for committing the resources necessary for the long-range planning and subsequent audit work necessary to independently and objectively reach valid conclusions and make meaningful recommendations for improving the operations of major Federal programs.

Thus, in our view, there is a need for a legislative change to provide GAO the authority it needs to gain access to tax information for use in evaluating the programs of non-tax administration agencies. The need for this change is most visible in the case of those programs that dispense financial aid or some other form of benefit. Such authority would, of course, be subject to the safeguards contained in current law. In this regard, GAO has demonstrated over an extended period its ability to safeguard the sensitive tax information that comes into its possession.

This concludes my prepared statement. We would be pleased to respond to any questions.

APPENDIX I.—OBJECTIVES, SCOPE, AND METHODOLOGY

This testimony is based on past and recent work GAO has done at the request of various congressional committees and subcommittees.

In March 1979, we issued a report to the Joint Committee on Taxation entitled "Disclosure and Summons Provisions of 1976 Tax Reform Act—Privacy Gains With Unknown Law Enforcement Effects" (GGD-78-110, Mar. 12, 1979). In that report, we pointed out that the disclosure provisions had afforded taxpayers increased privacy over information they provided IRS but had adversely affected IRS' ability to coordinate with other members of the law enforcement community. In December 1979 hearings before the Permanent Subcommittee on Investigations, Senate Committee on Governmental Affairs, on IRS' efforts to combat narcotics traffickers, we testified that changes to the disclosure provisions were needed.

In April 1980 hearings before the Senate Appropriations Subcommittee on Treasury, Postal Service, and General Government on changes needed to strengthen Federal efforts to combat narcotics traffickers, we proposed various administrative actions that IRS could take to expedite authorized disclosures of tax information to other agencies. We also reemphasized the need for legislative changes. In June 1980, we issued a report to that same Senate Appropriations Subcommittee entitled "Disclosure And Summons Provisions of 1976 Tax Reform Act—An Analysis of Proposed Legislative Changes" (GGD-80-76, June 17, 1980). We also testified on those proposed legislative changes in June 1980 before the Subcommittee on Oversight of the IRS, Senate Committee on Finance. In November 1981, we testified before the same Senate Subcommittee on S. 732—a bill which would amend the disclosure provisions.

The overall objective of the review we recently carried out for the House Ways and Means Oversight Subcommittee was to assess the operation and effects of the disclosure statute as it relates to taxpayer privacy and law enforcement. To accomplish our objective, we reviewed existing law, and the various legislative changes which have been proposed; the regulations, policies, and procedures followed by IRS and various law enforcement agencies concerning the disclosure of tax information; IRS' files which show the type of information which is and is not disclosed under current law, and the length of time it takes for information to be disclosed; statistics provided by IRS and other Federal agencies on disclosures made both before and since 1977 and on IRS' participation in Federal law enforcement efforts.

We interviewed various IRS national, regional, and district level officials responsible for controlling disclosures of tax information and for IRS participation in criminal investigations. We also interviewed Customs Service, Federal Bureau of Investigation, and DEA officials in headquarters and field offices; Department of Justice Strike Force attorneys in five cities—Boston, Kansas City, Los Angeles, Manhattan, and Miami; and U.S. attorneys in five districts—Boston, Dallas, Jacksonville, Los Angeles, and Manhattan. In addition, we had discussions with officials of two Inspector General Offices, three States' Attorney General offices, and the Central Intelligence Agency; and with representatives of the American Civil Liberties Union and the American Bar Association.

To determine the effects of the disclosures provisions on Federal law enforcement efforts, we compared the frequency with which IRS disclosed tax information prior to 1977 with the experience since the disclosure provisions took effect. Furthermore, for disclosures made pursuant to a Federal agency's request, we reviewed case files to assess the timeliness of the processes followed by IRS and the Department of Justice. We reviewed 100 percent of the requests on file at five IRS district offices. The time required for fulfillment of a request was determined by computing the number of calendar days which elapsed between the date IRS first became aware of a potential request (referred to by IRS as the prenotification date) and the date the disclosure actually was made.

We also reviewed use of the legal provision which allows IRS to initiate disclosure of certain types of information it possesses when that information indicates a Federal non-tax crime has been committed. To do this for the 16 months ended September 30, 1981, we reviewed all of IRS' national office case files, as well as all files in five IRS district offices pertaining to such disclosures. In doing so, we reviewed both the disclosures IRS made to the Department of Justice pursuant to this provision, and any information which IRS could not legally disclose to Justice.

In addition, we evaluated statistics provided to us by IRS concerning the pariticipation of its agents in joint Federal investigative efforts. By so doing, we sought to determine the effect current tax disclosure provisions have had on IRS' involvment in those activities.

COMPARATIVE ANALYSIS OF 26 U.S.C. §§6103, 7213, and 7217

WITH

H.R. 1502 AND THE ADMINISTRATION'S PROPOSAL

TAX DISCLOSURE PROVISIONS: COMPARISON OF 26 U.S.C. §6103, H.R. 1502 AND THE ADMINISTRATION'S PROPOSAL (note a)

CATEGORIES OF TAX INFORMATION

26 U.S.C. §6103

Existing law divides information into three categories: return, return information, and taxpayer return information.

(b) Definitions

(1) Return--any document the taxpayer is required by law to file, including information returns, declarations of estimated tax, claims for refund, and any schedules and attachments.

(2) Return information--(a) all information on the return; (b) all information IRS has concerning the return, (e.g., whether the return is being audited); (c) all data received or collected by IRS relating to the return and determination of tax liability; and (d) any background or written document on the determination not open for public inspection.

By definition, return information does not include data in a form which cannot be associated with, or otherwise identify, directly or indirectly, a particular taxpayer.

(3) Taxpayer return information--return information (as in (2)) which is filed with or furnished to IRS by or on behalf of the taxpayer.

---

a/This analysis is limited to the impact of the major provisions of H.R. 1502 and the Administration's proposal. The Administration's proposal was recently introduced in the Senate as S.1891. H.R. 1502's counterpart in the Senate is S.732.

H.R. 1502	ADMINISTRATION'S PROPOSAL
Proposal, by definition, divides information into return information and nonreturn information, eliminating the category of taxpayer return information.	Proposal divides information into two categories, investigative return information and investigative nonreturn information, for the purpose of disclosure under section 6103(i), disclosure to law enforcement officials. These definitions parallel the definitions of return information and nonreturn information in H.R. 1502. The definitions of return and return information in current law would govern disclosure for all other subsections of §6103, and the category of taxpayer return information is eliminated.
(b) Definitions	(b) Definitions
(1) Return information--(a) all documents within existing category of "return" and (b) any information provided to IRS by or on behalf of an individual taxpayer.	(1) Return--any document the taxpayer is required by law to file, including information returns, declarations of estimated tax, claims for refund, and any schedules and attachments.
(2) Nonreturn information--all other information IRS has relating to the return and tax liability.	(2) Return information--(a) all information on the return; (b) all information IRS has concerning the return, (e.g., whether the return is being audited); (c) all data received or collected by IRS relating to the return and determination of tax liability; and (d) any background or written document on the determination not open for public inspection. By definition, return information does not include data in a form which cannot be associated with, or otherwise identify, directly or indirectly, a particular taxpayer.
Proposal adds a new definition: (3) Individual taxpayer--includes any individual taxpayer and small corporation, partnership, association, union or other entity with no more than two members.	(3)(A) Investigative return information 1/--(a) all documents within existing category of "return" and (b) any information provided to IRS by or on behalf of an individual taxpayer. (B) Investigative nonreturn information--all other information IRS has relating to the return and tax liability. Proposal adds a new definition: (C) Individual taxpayer--includes any individual taxpayer and small corporation, partnership, association, union or other entity with no more than two members.

1/The definitions in the Administration's proposed section 6103(b)(3), investigative return information and investigative nonreturn information, apply only to subsection (i), governing disclosure to law enforcement officials.

GAO Comments

Under present law, information supplied to IRS by a taxpayer, or anyone acting on his behalf, generally is disclosed only pursuant to court order. This court order requirement applies to information supplied by corporate as well as individual taxpayers. Under H.R. 1502 and the Administration's proposal, the category of protected tax information would include: (1) all tax returns, and (2) any information supplied to IRS by, or on behalf of, individual taxpayers and one or two-person corporations, partnerships, or similar business entities. Information supplied to IRS by any business entity composed of more than two persons could be disclosed upon the written request of certain Government officials. We believe that information supplied to IRS by business entities, regardless of size, should remain on the same footing as information supplied by individual taxpayers. We would recommend, therefore, that any amendments to §6103 not draw a distinction between individual taxpayers and corporations, partnerships, associations, unions, or similar business entities.

Several factors underlie the rationale for this recommendation. First, the basis for distinguishing between two and three-person business entities has not been established. Second, recent court opinions, including those of the Supreme Court, do not support the proposition that corporations, unlike individuals, do not enjoy constitutional protections. And third, information supplied to IRS by persons in support of a corporate return may disclose information about individual taxpayers. This is true regardless of the size of the business entity involved. Finally, the matter of access to tax information in general should be placed in perspective. H.R. 1502 and the Administration's proposed amendments to section 6103 would facilitate access to all tax information. This would be accomplished primarily by lessening the standards for obtaining court orders and decentralizing the authority to request tax information. Corporate records could be disclosed under these mechanisms as readily as individual records.

The importance of the definitional section cannot be overstated since the definitional categories ultimately determine the degree of privacy afforded the taxpayer. Under present law, the statutory definitions are somewhat ambiguous and need clarification--a point recognized by both H.R. 1502 and the Administration's proposal. One alternative way to clarify the categories of tax information and at the same time provide comparable protection to corporate and individual taxpayers, would be to amend section 6103 to provide for only two categories of tax information: (1) return--to include all tax returns and information supplied to IRS by all taxpayers or anyone acting on their behalf, and (2) return information--to include all other information IRS has with respect to the taxpayer. From a technical standpoint, we note that use of the terms "return" and "return information," in lieu of H.R. 1502's terms "return information" and "nonreturn information," would minimize the need to make conforming amendments to those provisions in section 6103 which are unrelated to disclosure for law enforcement purposes, such as disclosure to the Census Bureau. In fact, it is for this reason that the Administration adopts separate definitions for disclosure to law enforcement officials under section 6103(i). We believe, however, that using a definitional category for §6103(i) different from the definitions governing the other subsections of §6103 may add to, rather than resolve, confusion.

GAO Suggested Statutory Language

Paragraph (1) of subsection (b), section 6103 of title 26, United States Code, should be amended to read as follows:

(1) Return The term "return" means:
(A) Any tax or information return, declaration of estimated tax, or claim for refund required by, or provided for or permitted under, the provisions of this title which is filed with the Secretary by, on behalf of, or with respect to any person, and any amendment or supplement thereto, including supporting schedules, attachments, or lists which are supplemental to, or part of, the return so filed, and
(B) Any information provided by or on behalf of the taxpayer to whom such information relates, including
(i) the nature, source, or amount of the taxpayer's income, payments, receipts, deductions, exemptions, credits, assets, liabilities, net worth, tax liability, tax withheld, deficiencies, over-assessments, or tax payments, and
(ii) any part of any written determination, or any background file document relating to such written determination (as such terms are defined in section 6110(b)) which is not open to public inspection under section 6110.
But such term does not include data in a form which cannot be associated with, or otherwise identify, directly or indirectly, a particular taxpayer.

Paragraph (2) of subsection (b), section 6103 of title 26, United States Code, should be amended to read as follows:

(2) Return information The term "return information" means any information which the Secretary collects, obtains, or receives (including whether a return was filed and whether the taxpayer's return was, is being, or will be examined or subject to other investigation or processing), or any part of any written determination or any background file document relating to such written determination which is not a return as defined in paragraph (1).
But such term does not include data in a form which cannot be associated with, or otherwise identify, directly or indirectly, a particular taxpayer.

Paragraph (3) of subsection (b), section 6103 of title 26, United States Code, the category "taxpayer return information," should be repealed.

COURT-ORDERED DISCLOSURES

26 U.S.C. §6103

(i) Disclosure for Administration of Federal Laws Not Relating to Tax Administration

(1) Non-tax criminal investigation:

- (A) Requires *ex parte* court order for disclosure of return or taxpayer return information to law enforcement agencies.
- (B) Application for order by head of Federal agency involved in law enforcement or in the case of the Department of Justice, the Attorney General, Deputy Attorney General, or Assistant Attorney General.

Ex parte order may be issued if

- (i) on the basis of reliable information, there is reasonable cause to believe a crime has been committed;
- (ii) there is reason to believe that the return is probative; and
- (iii) information cannot reasonably be obtained from another source.

H.R. 1502	ADMINISTRATION'S PROPOSAL
(i) Disclosure for Administration of Federal Laws Not Relating to Tax Administration	(i) Disclosure for Administration of Federal Laws Not Relating to Tax Administration
(1) Non-tax criminal investigation:	(1) Non-tax criminal investigation:
(A) Requires *ex parte* order for disclosure of "return information."	(A) Requires *ex parte* order for disclosure of "investigative return information."
(B) Application for order by Attorney General, Deputy Attorney General, Assistant Attorney General, U.S. Attorney, or Attorney in charge of organized crime strike force.	(B) Application for order by Attorney General, Deputy Attorney General, Associate Attorney General, Assistant Attorney General, U.S. Attorney, or Attorney in charge of organized crime stike force.
Ex parte order may be issued if	*Ex parte* order may be issued if
(i) on the basis of reliable information, there is reasonable cause to believe a crime has been, or is being, committed;	(i)(I) on the basis of reliable information, there is reasonable cause to believe a crime has been, is being, or will be committed.
(ii) information is sought exclusively for use in Federal criminal investigation; and there is	(II) information is sought exclusively for use in Federal criminal investigation; and there is
(iii) reasonable cause to believe information sought is relevant.	(III) reasonable cause to believe information sought is relevant; or
	(ii)(I) arrest warrant has been issued for an individual who is a fugitive from justice;
	(II) information is sought exclusively for use in locating such individual; and there is
	(III) reasonable cause to believe information sought is relevant.

GAO Comments

Under existing law, "return" and "taxpayer return information" can be disclosed only by court order, applied for by the heads of Federal law enforcement agencies. Taxpayer return information includes any information concerning the return supplied to IRS by either the taxpayer or anyone acting on the taxpayer's behalf. Under this provision, for example, an accountant's work papers provided to IRS during an audit can be disclosed for non-tax purposes only by court order.

Under H.R. 1502, ex parte orders would be required for disclosure of "return information." Under the Administration's proposal, ex parte orders would be required for the same information, referred to as "investigative return information." As a general proposition, all other information, including the records of business entities comprised of three or more persons would be disclosed on the request of certain Government officials. In our view, information supplied to IRS by any taxpayer or his agents should be disclosed only pursuant to a court order. (See p. II-3).

H.R. 1502 and the Administration's proposal would amend the criteria for obtaining a court order. According to Justice officials, under the existing criteria, law enforcement agencies are caught in a "catch-22" position. To obtain the order, they must show that there is reason to believe that the information sought from IRS is probative. The Department of Justice has testified to considerable difficulty in meeting this standard in that often it cannot show that the information is probative until it actually has the requested tax information. The proposals respond to this by amending section 6103(i)(1) to require the Justice Department to show instead that the information sought from IRS is relevant to a matter relating to the commission of the crime being investigated. While we recognize that the standard of "relevancy" is intended to be less demanding than the "probative" test of present law, we would recommend the Committee provide interpretive guidance about how the proposed criteria would differ in application from the requirements of current law.

Under the Administration's proposal, "investigative return information" can also be disclosed, pursuant to court order, for the purpose of locating a fugitive from justice. Existing law, as interpreted by the Justice Department, does not authorize such disclosure. We understand the need for this authorization. If adopted, however, we suggest amending the language to more clearly reflect that tax information obtained under this provision will be used only by Federal officials in locating fugitives.

Both proposals do away with the requirement that, to obtain a court order, the agency seeking disclosure from IRS first ascertain that the information is not available from another source. In recognition of IRS' primary responsibility to administer the tax laws and collect the revenue, the Committee could consider refining the amendments to recognize that if the law enforcement agency can obtain the information from another source in a timely manner, and without prejudicing enforcement, there is no persuasive reason why judicial process should be invoked to compel disclosure by IRS.

Under existing law, the authority to request tax information for law enforcement purposes, either by court order or written request, generally lies with the head of any Federal agency that enforces Federal criminal laws not involving tax administration. H.R. 1502 and the Administration's proposal would vest the authority to request a court order in a limited number of Government attorneys within the Department of Justice. The heads of Federal investigative agencies could no longer independently request tax information. We agree with this proposal. Restricting this authority to Justice officials would promote the coordination between IRS and Justice which is essential to efficient Federal law enforcement. In this manner, Justice could help prevent duplicative investigations, provide investigative guidance, and otherwise assist Federal law enforcement officials in developing successful cases. And, by placing this authority in Justice, a mechanism is provided to ensure that requests made under both sections 6103(i)(1) and (i)(2) meet the applicable statutory requirements. It should be made clear, however, that after obtaining tax information, Justice officials are authorized to redisclose tax information to other agencies necessarily involved in the criminal investigation. (See p. II-12).

Also, when information obtained under §6103(i)(1) is disclosed, we see no need for the requirement that Justice submit a written request for disclosure of less protected "return information" under §6103(i)(2). This is because in obtaining §6103(i)(1) information, Justice has already met more stringent criteria than that contained in §6103(i)(2).

DISCLOSING NONRETURN INFORMATION

26 U.S.C. §6103

(i)(2) Disclosure of return information other than taxpayer return information by written request of agency heads directly engaged in criminal law enforcement.

Such request shall include
- (i) name and address of the taxpayer,
- (ii) relevant taxable periods,
- (iii) statutory authority for the investigation or proceeding, and
- (iv) specific reason or reasons why such disclosure is or may be material to the proceeding or investigation.

Name and address of taxpayer disclosed pursuant to written request.

DISCLOSING NONRETURN INFORMATION

H.R. 1502	ADMINISTRATION'S PROPOSAL
(i)(2) Disclosure of nonreturn information on written request of agency heads and Inspectors General, and in the case of the Department of Justice, the Attorney General or his designee.	(i)(2) Disclosure of investigative nonreturn information on written request of agency heads and Inspectors General, and in the case of the Department of Justice, Attorney General, Deputy Attorney General, Associate Attorney General, Assistant Attorney General, U.S. Attorney, Attorney in charge of organized crime strike force, or a supervisory-level attorney designated by the Attorney General.
Such request shall include (i) name and address of the taxpayer, (ii) relevant taxable periods, (iii) statutory authority for the investigation or proceeding, and (iv) allegations of criminal conduct giving rise to the proceeding or investigation.	Such request shall include (i) name and address of the taxpayer, (ii) relevant taxable periods, (iii) statutory authority for the investigation or proceeding, and (iv) allegations of criminal conduct giving rise to the proceeding or investigation.
Name, address, social security number of taxpayer, whether a taxpayer filed a return, and whether there is or has been a criminal investigation of taxpayer disclosed pursuant to written request.	

GAO Comments

Under existing law, information which can be disclosed on written request of an agency head is limited to information which is not considered taxpayer return information. H.R. 1502 would allow all "nonreturn information" to be disclosed upon written request of certain Government officials. The Administration's proposal would allow the same information, referred to as "investigative nonreturn information," to be disclosed upon written request. As discussed on page II-3, the category of protected information under both proposals seems too narrow. The proposals would allow Government officials to gain access by written request to some categories of information that, in our opinion, should be protected and disclosed only via court order.

Under present law, the written request must state the specific reason why disclosure is or may be material to the criminal investigation. Both proposals amend this to simply require an allegation of criminal conduct giving rise to the proceeding or investigation. This amendment should alleviate the so-called "catch-22" situation, discussed on page II-7, in the case of written requests.

We do not agree with the provision in both H.R. 1502 and the Administration's proposal to allow all agency heads and Inspectors General to gain access to tax information by written request. This authority should be restricted to Justice officials to ensure effective coordination between IRS, Justice, and other Federal agencies. (See p. II-7). Justice officials, however, should be clearly authorized to redisclose tax information to other agency heads and Inspectors General when necessary. (See p. II-12.) We agree with the provision in H.R. 1502 which would allow the Attorney General to delegate this authority to those officials who need access to tax information by written request. Under this proposal, the Attorney General could authorize U.S. attorneys and heads of organized crime strike forces to gain access via written request. Conversely, the Attorney General could subsequently withdraw that authorization as necessary. The Administration's proposal would allow all Justice officials authorized to apply for a court order, as well as supervisory-level attorneys designated by the Attorney General, to submit written requests for tax information.

Under H.R. 1502, Government officials could also find out, by written request, whether a taxpayer filed a return and whether there is or has been a criminal investigation of a taxpayer. This is a needed amendment to section 6103. In the interest of efficiency and economy, law enforcement officials should first know if IRS has potentially useful information on the taxpayer before seeking a court order.

REDISCLOSURE OF TAX INFORMATION

26 U.S.C. §6103

Tax information obtained under (i)(1) and (i)(2) may be redisclosed to any Federal employee directly engaged in the criminal proceeding.

H.R. 1502	ADMINISTRATION'S PROPOSAL
Explicitly authorizes a Government official to redisclose return and nonreturn information obtained either under (i)(1) or (i)(2) to such other Federal government personnel, or witness, he deems necessary to assist him during the criminal proceeding.	Explicitly authorizes a Government official to redisclose investigative return information or investigative nonreturn information obtained under (i)(1), (i)(2) or (i)(3) to such other Federal government personnel, or witness, he deems necessary to assist him during the criminal proceeding.

GAO Comments

The proposed amendments to §6103 would make clear that Government officials are authorized to redisclose tax information to those necessarily involved in the criminal investigation, including prosecutive witnesses. We agree with this proposal. For example, it is sometimes necessary for prosecutors to disclose evidence to a witness during an investigation or in preparation for a criminal proceeding. However, we have recommended that the authority to make written requests for tax information be limited to the Justice Department. (See p. II-11). If that recommendation is accepted, this redisclosure provision may have to be modified to specifically authorize Justice to redisclose tax information to agencies on whose behalf the Department makes written requests. Also, in our view, the law should require an accounting for all redisclosures made under this provision.

IRS-INITIATED DISCLOSURE OF NON-TAX CRIMINAL INFORMATION

26 U.S.C. §6103

(i)(3) IRS may disclose information other than taxpayer return information to agency heads where there is evidence that a Federal crime has been committed. Name and address of taxpayer can be disclosed under this provision if return information is available.

H.R. 1502	ADMINISTRATION'S PROPOSAL
(i)(3)(A) Places legal duty on IRS to disclose nonreturn information where there is evidence of a Federal crime. Name and address of taxpayer can also be disclosed under this provision.	(i)(3)(A) Places legal duty on IRS to disclose investigative nonreturn information where there is evidence of a Federal crime. For purposes of this provision, where disclosure would involve information supplied by or on behalf of a corporation, partnership, association, trust, estate or other legal entity, there must be reasonable cause to believe such entity was formed, or is being operated or maintained, for the purpose of facilitating or engaging in Federal criminal activity. Name and address of taxpayer can also be disclosed under this provision.
(B) When IRS makes a prosecutive recommendation to Justice involving a Federal tax crime, any return or nonreturn information evidencing a non-tax Federal crime must also be disclosed.	(B) When IRS makes a prosecutive recommendation to Justice involving a Federal tax crime, any investigative return information or investigative nonreturn information evidencing a non-tax Federal crime must also be disclosed.
IRS may decline to disclose any information under the above paragraphs if disclosure would identify a confidential informant or seriously impair a civil or criminal tax investigation.	IRS may decline to disclose any information under the above paragraphs if disclosure would identify a confidential informant or seriously impair a civil or criminal tax investigation.

GAO Comments

H.R. 1502 and the Administration's proposal place an affirmative legal duty on IRS to provide law enforcement agencies information that "may constitute evidence of a violation of Federal criminal laws." The scope of this duty needs clarification. As presently drafted, the proposals could contemplate a responsibility, even in the absence of a request, for IRS to regularly review its files for non-tax criminal evidence. Recognizing that IRS' primary responsibility is tax administration, we believe IRS' disclosure obligation should only extend to non-tax criminal information it becomes aware of during the normal course of administering the tax laws.

The Administration's proposal would distinguish between information supplied by or on behalf of legitimate businesses and information supplied by or on behalf of businesses engaged in "illegal" activities. Under the proposal, IRS must disclose criminal information supplied the Service by or on behalf of any business entity "formed, . . . operated or maintained with a purpose of facilitating or engaging in Federal criminal activity." Investigative nonreturn information supplied by a legitimate business, primarily its books and records, could not be unilaterally disclosed to the Justice Department. We disagree with this proposal for several reasons. First, in our view, information supplied to IRS by any taxpayer or his agents should be disclosed only pursuant to a court order. (See p. II-3). Second, under the proposal, information supplied to IRS by an "illegal" business comprised of one or two persons could not be disclosed, whereas similar information supplied by a larger "illegal" business must be disclosed. We see no rationale for this distinction. Third, §6103 is made confusing by incorporating a distinction between legal and illegal business entities solely for purposes of this subsection. Fourth, it is unclear how IRS would be able to effectively distinguish between legal and illegal businesses. And finally, if IRS were authorized to apply for a court order to disclose protected information, as we recommend below, such a distinction may be unnecessary.

H.R. 1502 and the Administration's proposal would also require IRS to disclose criminal evidence on non-tax matters to Justice when making prosecutive recommendations in a tax case. This would allow necessary coordination within the Department, providing Justice officials with the needed flexibility to decide how to proceed against a certain individual, and helping to avoid problems stemming from the Department's dual prosecution policy.

We recognize the need expressed in both proposals to enable IRS to provide assistance to law enforcement agencies. Under present law, when IRS uncovers criminal evidence based on taxpayer return information, it lacks authority to report it to the appropriate law enforcement agency. The proposed amendments to section 6103 do not resolve this problem. Under H.R. 1502, IRS would not be authorized to unilaterally inform law enforcement officials when it had criminal evidence based on return information. And, under the Administration's proposal, IRS could not unilaterally disclose investigative return information. We suggest, therefore, that the Congress authorize IRS to apply for a court order to disclose protected information. Such a provision would ensure that a neutral third party--the judiciary--decides on the disclosure of such information.

GAO Suggested Statutory Language

Paragraph (3) of subsection (i), section 6103 of title 26, United States Code, should be amended to read as follows:

(3) Disclosure of information concerning possible criminal activities.

(A) Information from taxpayer: Upon application by the Secretary, a U.S. District Court may, by ex parte order, direct that a return (as defined in section 6103(b)(1)) be disclosed to the head of the appropriate Federal investigative agency if, in the opinion of the court, such information is material and relevant to a violation of Federal criminal law.

(B) Application for order: The application for an ex parte court order shall set forth the name of the taxpayer involved; the time period to which the request relates; and the reasons why, in the opinion of the Secretary, the information is material and relevant to a violation of Federal criminal law.

(C) Procedures: A U.S. District Court shall act upon any application for an ex parte order within 5 days of the receipt thereof. In the event that the district court denies the application

(i) a motion for reconsideration shall be acted upon not later than 5 days after the receipt of such motion, and

(ii) an appeal shall be disposed of as soon as practicable but not later than 30 days after receipt of appeal.

(D) Duty of the Secretary: The Secretary or his designee shall disclose, to the head of the appropriate Federal investigative agency, information ordered disclosed pursuant to this subsection.

(E) Further Disclosure: The head of the Federal investigative agency may further disclose any information, which has been disclosed to him pursuant to an ex parte order, to such other Government personnel or witness as he deems necessary to assist him during or in preparation for any administrative, judicial, or grand jury proceeding or in a criminal investigation which may result in such a proceeding.

(F) Return Information: The Secretary may disclose in writing return information which may constitute evidence of a violation of Federal criminal laws to the extent necessary to apprise the head of the appropriate Federal agency charged with the responsibility for enforcing such laws. For purposes of this subsection, the name and address of the taxpayer shall not be treated as a return if there is return information which may constitute evidence of a violation of a Federal criminal law.

USE OF TAX INFORMATION IN JUDICIAL OR ADMINISTRATIVE PROCEEDINGS

26 U.S.C. §6103

(i)(4) Any information obtained under (i)(2) or (i)(3) may be entered into evidence in any administrative or judicial proceeding involving a non-tax Federal crime. Information obtained under (i)(1) may be entered into evidence upon the court's finding that the information is probative.

H.R. 1502	ADMINISTRATION'S PROPOSAL
(i)(4) Any information obtained under (i)(1), (i)(2) or (i)(3) may be entered into evidence in any administrative, judicial, or grand jury proceeding involving a non-tax Federal crime or any ancillary civil proceeding by order of the court.	(i)(4) Any information obtained under (i)(1), (i)(2) or (i)(3) may be entered into evidence in any administrative or judicial proceeding involving a non-tax Federal crime, or any ancillary civil proceeding, unless the Secretary determines, and the court agrees, that such admission would identify a confidential informant or seriously impair a civil or criminal tax investigation.

GAO Comments

H.R. 1502 and the Administration's proposal provide a needed authorization for redisclosure of tax information in connection with civil actions initiated under civil rights, antitrust, fraud, and organized crime statutes. It also could be invoked for other civil statutes that have a criminal counterpart. It should be recognized, however, that the authorization may not apply to organized crime and antitrust cases where the Government elected to proceed solely on a civil basis, as in a civil forfeiture action under 21 U.S.C.§881. This is because the provision provides no mechanism to transfer tax related information where the judicial action is exclusively civil, and there is no ancillary criminal proceeding or criminal investigation. The Congress may want to consider the desirability of such an authorization.

DISCLOSURE UNDER EMERGENCY CIRCUMSTANCES

26 U.S.C. §6103	H.R. 1502 and ADMINISTRATION'S PROPOSAL
No comparable provision.	Adds a new paragraph (5) to subsection (i) Emergency circumstances: Under emergency circumstances involving an imminent danger of physical injury to any person, serious physical damage to property, or flight from prosecution, IRS may disclose any necessary information to the appropriate Federal agency. IRS must then notify Justice, and Justice must notify the District Court after such disclosure has been made.

GAO Comments

We support the intent of this provision, which provides the Secretary discretionary authority to disclose information in emergency circumstances. We would, however, include the threat to national security in the emergency circumstances identified in the proposal. On the other hand, this provision could be more narrowly drawn and still achieve its intent. As discussed on page II-14, the Secretary should, in our view, be given the authority to seek court-ordered disclosure when IRS uncovers criminal evidence based on a return. In light of this, we suggest that the emergency circumstance disclosure authority be explicitly keyed to the Secretary's inability to obtain a court order in sufficient time to prevent physical harm to persons, physical damage to property, harm to national security, or flight from prosecution. We also would suggest expanding this authority to allow disclosure of criminal evidence to appropriate State authorities since some emergency circumstances, such as murder, would involve State crimes.

GAO Suggested Statutory Language

Subsection (i), section 6103 of title 26, United States Code, should be amended to add a new paragraph:

Emergency Circumstances

(A) Under emergency circumstances, the Secretary or his designee may disclose such information, including returns, as is necessary to apprise the appropriate Federal or State authorities having jurisdiction over the offense or matter to which such information relates.

(i) "Emergency circumstances" means circumstances involving an imminent threat of harm to persons, property, or national security, or flight from prosecution, and in which, in the judgment of the Secretary, time is insufficient to obtain an *ex parte* order authorizing disclosure of the information involved.

(B) The Secretary shall maintain standardized records or accountings of all disclosures made under this paragraph.

ASSISTANCE OF IRS IN JOINT TAX/NON-TAX INVESTIGATIONS

26 U.S.C. §6103	H.R. 1502 and ADMINISTRATION'S PROPOSAL
No comparable provision.	Adds a new paragraph (6) to subsection (i) No portion of §6103 precludes or prevents IRS from assisting Federal agencies in joint tax/non-tax criminal investigations.

GAO Comments

We anticipate that IRS and Justice will encounter considerable difficulty administering this provision, and recommend the intended operation of this section be clarified. The precise purpose of the authorization, and the uses to which it may be put, should be defined with greater descriptive clarity. Although the proposal states that nothing in section 6103 shall be construed to preclude or prevent IRS' assistance in joint tax/non-tax criminal investigations, it is not clear what type of IRS "assistance" is envisioned, what might qualify as a "joint tax/non-tax" investigation, or whether the authorization is intended to override the disclosure restrictions set forth elsewhere in section 6103. Assuming the existence of a joint investigation, for example, would IRS still be obliged to await a court order or written request to disclose evidence of non-tax offenses in its files? On the other hand, this authorization may be intended simply to encourage IRS' participation in joint investigations but only within the framework of the disclosure restrictions prescribed by section 6103. This could be viewed as consistent with other provisions of the proposals which, among other matters, modify present law to explicitly authorize IRS to disclose non-tax criminal information to Justice when making a tax case.

In addition, the Congress may want to consider two problems under existing law which are not specifically addressed in either H.R. 1502 or the Administration's proposal. Under §6103(h)(2), which authorizes disclosures to Justice for tax administration purposes, IRS can disclose tax information to Justice when referring a tax case for prosecution. IRS has interpreted this provision as precluding the disclosure of tax information, either in a tax or a joint tax/non-tax criminal case, prior to case referral. Prereferral disclosure in tax cases is essential, however, to ensure effective coordination between IRS and Justice in prosecuting criminal tax matters, and to obtain such advice as may be necessary to develop the tax case. In addition, §6103 should be clear in authorizing such disclosure to both U.S. attorneys and strike force attorneys.

DISCLOSURE TO STATE OFFICIALS

26 U.S.C. §6103

No comparable provision.

H.R. 1502	ADMINISTRATION'S PROPOSAL
Adds a new paragraph (7) to subsection (i)	Adds a new paragraph (7) to subsection (i)
Provides authorized officials with authority to obtain an *ex parte* court order authorizing the redisclosure of tax information which evidences a violation of a State felony statute. Under this provision, a court can authorize redisclosure to a State attorney general or a district attorney upon finding that (A) on the basis of reliable information, there is reasonable cause to believe a State felony has or is occurring; and (B) there is reasonable cause to believe that the information is relevant.	Provides authorized officials with authority to obtain an *ex parte* court order authorizing the redisclosure of tax information which evidences a violation of a State felony statute. Under this provision, a court can authorize redisclosure to a State attorney general or a district attorney upon finding that (A) on the basis of reliable information, there is reasonable cause to believe a State felony has, is, or will occur; and (B) there is reasonable cause to believe that the information is relevant; and (C) information will be disclosed exclusively for use in a state criminal investigation or proceeding.
	The court shall not order disclosure if the Secretary determines and certifies to the court, and the court agrees, that such disclosure would identify a confidential informant or seriously impair a civil or criminal tax investigation.

GAO Comments

Present law does not authorize the redisclosure of tax information concerning non-tax State crimes. H.R. 1502 and the Administration's proposal would authorize certain Federal officials to obtain an *ex parte* court order authorizing redisclosure when the information relates to State felony violations. Although there is a need for this redisclosure authorization, we would suggest a modification to this section to accommodate privacy concerns. Redisclosure should be made only to State attorneys general. The attorneys general would, of course, be authorized to further redisclose the information as necessary to carry out their specific criminal enforcement responsibilities. Also, IRS should be notified of redisclosures to State attorneys general, as well as any redisclosures made by these State law enforcement officials.

DISCLOSURE TO COMPETENT AUTHORITY UNDER INTERNATIONAL CONVENTIONS AND TREATIES

26 U.S.C. §6103

(k)(4) Disclosure of tax information to foreign governments to extent authorized under tax conventions.

H.R. 1502	ADMINISTRATION'S PROPOSAL
(k)(4) Adds an authorization for the disclosure of tax information to extent authorized under mutual assistance treaties. Requires ex parte court order for disclosure of information involving non-tax criminal matters under mutual assistance treaties, based on finding that (A) there is reasonable cause to believe that information is relevant to the commission of a specific criminal act that has been or is being committed against laws of the foreign country; and (B) information is sought exclusively for use in a foreign country's criminal investigation or proceeding concerning such criminal act.	Adds a new paragraph (8) to subsection (i), authorizing the disclosure of tax information to extent authorized under mutual assistance treaties. Requires ex parte court order for disclosure of information involving non-tax criminal matters under mutual assistance treaties, based on finding that (A) there is reasonable cause to believe that information sought may be relevant to the commission of a specific criminal act that has been or is being committed against non-tax laws of the foreign country; and (B) information is sought exclusively for use in a foreign country's investigation or proceeding concerning such criminal act. Court shall not disclose any information under this provision if Secretary determines, and certifies to the court, that such disclosure would identify a confidential informant or seriously impair a civil or criminal tax investigation.

GAO Comments

The proposals provide a needed mechanism to allow the Government to perform according to mutual assistance treaties it has entered into with foreign governments to exchange criminal evidence. Under these provisions, a court order is required for all disclosures, which we believe adequately accommodates privacy concerns. Also, it should be noted that under mutual assistance treaties generally, evidence exchanged with foreign governments must relate to criminal acts which are considered crimes in both countries involved, and there is considerable discretion provided in the treaties not to disclose any information which would be contrary to the public interest of the governments involved. These safeguards should protect against abusive disclosures.

FOREIGN INTELLIGENCE ACCESS

26 U.S.C. §6103 and H.R. 1502	ADMINISTRATION'S PROPOSAL
No comparable provision.	Adds a new paragraph (9) to subsection (i) Investigative return and investigative nonreturn information may be disclosed to the Attorney General and may be redisclosed to personnel of a Federal intelligence agency upon the personal certification of the Attorney General that the information is sought exclusively for use in foreign intelligence collection or a foreign counter-intelligence investigation and that there is reasonable cause to believe, based upon information believed to be reliable, that the subject of the information is, or may be-- (A) engaged in espionage, sabotage, clandestine intelligence activities, or international terrorism pursuant to the direction of a foreign power; (B) the actual target of an active effort by a foreign intelligence service or international terrorist organization involving positive steps to accomplish recruitment; or (C) furnishing or about to furnish national defense information, sensitive economic or technological information or materials, or foreign policy information to a representative of a foreign power or foreign intelligence service.

GAO Comments

The Administration's proposal would allow for disclosure of tax information to the Attorney General for use in foreign intelligence collection or foreign counter-intelligence investigations. Disclosure is authorized on the personal certification of the Attorney General that the criteria listed above is met. The Attorney General would be further authorized to redisclose such tax information to Federal intelligence agencies.

The need for this disclosure authorization should be closely scrutinized by the Congress for several reasons. First, under both current law and the Administration's proposal, the Attorney General can gain access to tax data for non-tax criminal investigative purposes via court order or written request. Thus, the Attorney General already has the authority to seek disclosure of tax information to assist in investigations involving espionage, sabotage, international terrorism, and other crimes. Second, another portion of the Administration's proposal which we support would authorize disclosures of tax information under emergency circumstances. We have suggested that threats to national security be included under that provision. By adopting that suggestion, the Congress would further alleviate the need for a separate intelligence-related disclosure authorization. Finally, we question whether adequate privacy safeguards have been built into this particular proposal. While the Attorney General would be required to certify a need for the tax information, no neutral third-party--such as a court--would be involved.

Chairman **Rangel**. I want to thank you. Your recommendations do make a lot of sense, and your statement kind of answers for the first time some of the problems that we have in reaching a common ground that assists law enforcement, while at the same time does not violate the rights of privacy. We may be asking you to do some more work for us relating to perceptions that Justice Department people have as to what the law is. It may mean we have to educate rather than legislate. There is no sense changing the law merely because of other people's perceptions about existing law.

Mr. Pickle.

Mr. **Pickle**. I do not have any questions. I have not had a chance to read all of your statement. I am looking at the summary now.

I would observe, though, that you have pointed out that we need to have better coordination, at least coordination has been adversely affected since this change was made, and you do offer some six or seven different suggestions.

They seem to be reasonable suggestions, and while I have not been able to hear all the testimony this morning, your testimony would be helpful to us and we thank you.

Chairman **Rangel**. Mr. Crane.

Mr. **Crane**. Thank you, Mr. Chairman. I, too, want to express appreciation for the testimony.

There was a question that I posed earlier to some witnesses, and I was not altogether sure that I got the right answer. If I were employed by the IRS investigating a matter involving taxes, and in the process I found some quite compelling evidence that a major crime had been committed, but not a violation of the Tax Code, am I, as a private citizen, under existing law, required to report such finding to appropriate authorities without being an accessory after the fact?

Mr. **Anderson**. Before I turn that over to our counsel here, sir, to deal with it from a legal standpoint, I presume you understood from the dialog this morning, that there are instances in fact where the IRS agent could do something about it with respect to information that is not taxpayer return information, that is where the information has been obtained from a source other than the taxpayer or his agent. So far in calender year 1981, for example, there have been 81 instances in which an IRS agent thought he saw information like that, and in 46 of those 81 instances it was determined by IRS that the information was releaseable under the Tax Reform Act.

Mr. **Crane**. Does he have to seek a release? He might want an expert to give him an opinion, but I am just trying to think that if I were a private citizen, and I thought I saw a murder committed, say, and it so happened that the person who committed the murder robbed the murdered person, and if he reported on his income tax form that he stole in the commission of that murder, and reported it as income upon which he paid taxes, am I bound as a citizen to adhere only to the confidentiality of records with respect to any potential tax violation, as in this case, and pretend I never knew a murder had been committed?

Mr. **Anderson**. Let me have Ken Mead here try to speak to that.

Mr. **Mead**. The offense you described wouldn't be accessory after, or before the fact.

It would be a misprision of felony. At least, that would be the term in the Federal system. But prosecutors, if the case were ever to come up concerning an IRS employee in such a situation, would have to demonstrate almost conclusive knowledge on the part of the person, the agent that came across this information, before the agent could be found guilty of a misprision of felony. In the context of the Tax Reform Act of 1976, however, the misprision of felony statute would be superseded by the specific provisions of the 1976 act, and there are some circumstances under the 1976 act in which an agent could not legally disclose evidence of a criminal offense outside of his agency, unilaterally.

Mr. **Anderson**. Mr. Crane, the penalties under section 6103, of existing law are so severe for disclosure, improper disclosure of tax information, as to really stifle and really make people within the IRS extremely apprehensive of releasing information that is to be closely held, and subjecting themselves to those penalties.

Mr. **Crane**. I am trying to create a situation where it is not a tax matter.

Mr. **Anderson**. If the information on this nontax crime was obtained either from the taxpayer's return or other information provided by the taxpayer or the taxpayer's agent or representative, so as to require close-hold treatment by the IRS, then that is the type of information an IRS employee could not release.

If however, the IRS heard it from an informant providing information on the taxpayer, under existing law that information could be passed along. The distinction that is made in the law is between the fifth amendment-type information that the taxpayer or the taxpayer's representative provides and information obtained from other sources.

Mr. **Crane**. Another hypothetical situation. If, as an IRS agent, I knew that someone was engaged in the illicit drug trade, was making dollars that he was reporting on his income and paying taxes and faithfully observing the law in that regard, is there no way in which that information that I hold, indicating that this man is earning his money through illicit drug trafficking could be passed on to appropriate authorities in drug enforcement or justice under present law?

Mr. **Anderson**. That is not a hypothetical case, sir. Tax returns have been identified where the occupation listed was "trafficking in narcotics," and where under income, was shown "net profits in dealing in controlled substances."

Those terms have actually shown up on tax returns and IRS, under the law, given the source of that information, was unable to pass it along to the proper law authorities.

Mr. **Mead**. If an informant had given the agent the information about the trafficker, the agent could disclose that information. I would assume he would have to go through the bureaucracy at IRS and so forth. However, if the trafficker had told the agent during a tax examination or indicated such on the return, or if the trafficker's accountant or attorney had told the agent, then unilateral disclosure would be improper.

However, the Justice Department or the Drug Enforcement Administration, which is part of the Justice Department, could initiate the ex parte court-ordered disclosure procedure if it had reason to believe that IRS had such information.

Mr. CRANE. In this breakdown, we have existing law which says the IRS is authorized but not required to disclose return information that may constitute evidence of a violation of Federal criminal laws.

Is this not a discretionary power to release the kind of information I just described on the part of the IRS?

Mr. ANDERSON. The information that they are authorized to disclose at present is one of the three categories of tax information that exists, the one that is the least privileged. It would not encompass the return or taxpayer return information.

Mr. CRANE. One final question. We had testimony earlier today by Commissioner Alexander and Commissioner Kurtz on a point which both of them stressed, and that is the accessibility of a court order. They never knew of any instance, neither of them, in their experience, where a court order had been denied. Commissioner Alexander indicated that he felt that there is some basis for criticizing cumbersome red tape, causing unnecessary delays, and Commissioner Kurtz tended to agree with that.

Do you share that same view?

Mr. ANDERSON. First, I have seen statistics that indicate that there have been some declinations in the past. I saw a document that cited about 450 requests for ex parte court orders for tax information and three declinations by the courts. It does happen.

U.S. attorneys see a lot of problems pursuing access to tax information. Twenty percent of U.S. attorneys have never even tried.

Some statistics indicate 43 percent of all requests for court orders have come from only seven U.S. attorneys. So some U.S. attorneys have found it possible to work within the existing law in obtaining access, but there is a perception that is affecting the actions of a number of U.S. attorneys that it is not worth the effort to try to demonstrate the probativeness of the information desired, or to meet the other requirements of the law to obtain an ex parte court order.

Mr. CRANE. Thank you very much.

Chairman RANGEL. Mr. Duncan.

Mr. DUNCAN. I have no questions.

Chairman RANGEL. Does the General Accounting Office itself have any problems with the disclosure restrictions in doing your work as it relates to your congressional mandate?

Mr. ANDERSON. We believe we could be serving the Congress more fully and effectively with a little additional access.

We have prepared a paper on that topic and rather than recite it in detail here, I will provide that for the record.

Chairman RANGEL. Thank you.

[The information follows:]

THE U.S. GENERAL ACCOUNTING OFFICE NEEDS GREATER ACCESS TO TAX INFORMATION TO FULFILL ITS AUDIT AND EVALUATION RESPONSIBILITIES

GAO IS THE AUDIT ARM OF THE CONGRESS

GAO assists the Congress in overseeing and improving Federal Government operations. The overall objective of GAO's audits and evaluations is to bring about improvements in the management and conduct of Federal programs and to evaluate ways of making both proposed and ongoing Federal programs operate more effectively, efficiently, and economically. Specifically, GAO seeks to improve Government operations by providing answers to such questions as whether: Federal funds are being spent legally; Federal programs are achieving their objectives; alternative ways exist for accomplishing program objectives at lower costs; waste and inefficient use of public money can be eliminated; and the accounting and financial reporting systems are adequate.

As the audit arm of the Congress, GAO serves a vital role for the Legislative Branch by overseeing Executive Branch programs and expenditures. However, current law does not provide GAO with the degree of access to tax returns and return information needed to carry out its full range of legislatively authorized audits and evaluations.

GAO NEEDS GREATER ACCESS TO TAX RETURN INFORMATION TO FULFILL ITS RESPONSIBILITIES

In establishing GAO, the Congress recognized that the Office would need complete access to the records of the Federal departments and agencies so it could make independent audits of their programs and operations. Thus, the Budget and Accounting Act of 1921 and various other statutes provide GAO with broad and comprehensive authority to gain access to the records of Federal departments and agencies. This authority extends not only to accounting and financial auditing but also to administration, operations, and program evaluation. Notwithstanding this broad authority, GAO has had only limited legal access to tax returns and return-related information.

The Accounting and Auditing Act of 1950, as amended October 7, 1977, by Public Law 95-125, and 26 U.S.C. § 6103(i)(6) give GAO access to tax returns and return information for the specific purpose of auditing the Internal Revenue Service (IRS) or the Bureau of Alcohol, Tobacco and Firearms (BATF). For audits of agencies other than IRS or BATF, GAO's only basis for access to tax returns or return information is through 26 U.S.C. § 6103(f)(4). This provision authorizes the Joint Committee on Taxation, the House Committee on Ways and Means, and/or the Senate Committee on Finance to obtain tax returns through designated agents. Thus, GAO can gain access to tax returns when working as a designated agent of one of those committees.

Through these authorizations, GAO is able to effectively plan, conduct, and report on audits of most Federal tax administration activities. An exception lies with audits of those activities involving tax return information exchanged pursuant to tax treaties between the United States and foreign nations. Nearly all tax treaties contain a secrecy clause prohibiting disclosure of tax return information except for purposes of tax assessment, collection, prosecution, or enforcement. Thus, neither GAO nor the Congress can effectively oversee IRS' international operations and activities. Further, because this limited access results from treaty provisions mutually agreed to by the U.S. and foreign countries, it appears that congressional action to legislate broader access would have limited practical consequence if these foreign countries were not amenable to exchanging tax data pursuant to treaty or otherwise.

The access problem is most severe, however, in its impact on GAO's ability to effectively audit the Executive Branch's non-tax adminsitration activities. Tax return information is essential to GAO in auditing and evaluating many non-tax administration activities, particularly those where the reported income of program participants is needed in determining whether the program is meeting congressional intent and/or in evaluating how efficiently and economically the program is being managed. On occasion, GAO has been able to obtain tax return information for these purposes by conducting an audit as the designated agent of one of the previously mentioned tax-writing committees. This arrangement, however, is not a satisfactory solution to the problem because it does not provide GAO with the permanent authority necessary to effectively carry out its role and responsibilities. GAO lacks a sufficiently solid basis for committing the resources necessary for the long-range planning and subsequent audit work necessary to independently and objectively reach valid conclusions and make meaningful recommendations for improving the operations of major Federal programs.

With expanded access to tax returns and return-related information, GAO could become a more effective tool for the Congress. GAO would be better able to carry out the full range of audits and reviews necessary for improved oversight. However, it is important that any amendments expanding GAO access retain the statutory and procedural safeguards that presently apply to the handling of tax information obtained during a GAO audit of tax administration activities. These safeguards include procedural and committee approvals requisite to GAO access to tax data; legislative restrictions on GAO disclosure of such data; and civil and criminal sanctions against unauthorized disclosure.

Some examples follow of how GAO could bring expanded access to tax returns to bear in its assessments of program effectiveness, efficiency and economy.[1]

Assessing program effectiveness

GAO's assessments of program effectiveness are aimed at determining whether the programs are achieving their legislatively mandated objectives. As part of these studies, GAO attempts to determine whether (1) management weaknesses have adversely affected the achievement of desired objectives, (2) alternative approaches might achieve program objectives more effectively or at lower cost, and (3) benefits or detriments are occurring that were not contemplated when the program was established. In some cases, GAO's findings may justify recommending that the Congress reconsider the program objectives in the light of experience with the program.

Greater access to tax return information would enable GAO to develop or corroborate economic and social characteristics for those segments of our population that are the focus of Federal programs or policies. Access would also permit independent and impartial testing and validation of different hypotheses that the Congress or the Executive Branch may have used in establishing public policy. The application of these evaluation methods and the reporting of the results to the Congress would provide legislators with more and better information for determining the extent a program is meeting its original objectives and what changes might be in order.

Assessing program efficiency and economy

GAO's assessments of the efficiency and economy with which Federal programs are carried out involve examining compliance with laws and regulations, identifying opportunities to achieve program objectives at less cost, and evaluating the adequacy of internal controls and financial reporting. Access to tax return information is needed by GAO for the purpose of reviewing Federal programs where such information is or could be used to establish eligibility, administer the distribution of program benefits, or otherwise determine whether Federal programs are being carried out as intended by the Congress. Examples of programs where tax information would be useful for the above purposes include retirement, disability, and related compensation programs, as well as most needs-based programs such as food stamps, subsidized housing, Aid to Families with Dependent Children, and many others.

Assessing Social Security Administration programs: a case in point

GAO has been auditing and evaluating programs carried out under the Social Security Act for many years and, during that time, the Congress and the Executive Branch have used GAO reports to eliminate inefficiency and waste and reduce program benefits found to be unneeded or not meeting their objectives. However, in March 1981, IRS advised the Social Security Administration (SSA) that earnings information gathered and used by SSA to administer its programs is tax return information and, therefore, is not to be disclosed to GAO due to the restrictions imposed by the Tax Reform Act of 1976. IRS told SSA that GAO could only have access to perform its reviews if it was acting as a designated agent of one of the appropriate committees of the Congress. IRS stated that "Under no other instances can you disclose tax information to GAO acting on their authority even if they assert that it is needed to conduct an audit of SSA's administration of the Social Security Act."

So that GAO would not have to terminate its important work at SSA and related agencies administering programs under the Social Security Act, the Chairman of the House Ways and Means Committee temporarily designated GAO as the

---

[1] GAO's responsibilities extend beyond its audit role to debt collection and claim settlement. While these activities are beyond the scope of this paper, there have been numerous proposals to use tax information and the internal revenue laws to facilitate debt collection and claims settlement efforts to all Federal agencies, including GAO. This topic has been addressed through several recent congressional hearings at which GAO has testified and is the subject of legislation now pending in various House and Senate committees.

Committee's agent. In doing so, the Chairman recognized that "this is intended to be a temporary resolution of GAO's status under the Code's disclosure provisions until a legislative solution can be effected."

LEGISLATIVE REMEDY IS NEEDED

It is apparent from the foregoing discussion that GAO's ability to provide the Congress with needed information on the operations of major Federal programs could be significantly enhanced by broadening its legal access to tax returns and return-related information. GAO has demonstrated over an extended period its ability to appropriately safeguard the sensitive information that comes into its possession. For these reasons, we believe that it would serve the Congress' purposes to amend 26 U.S.C. § 6103 so as to extend GAO's access to tax information for certain purposes beyond those currently authorized.

An exception concerns tax information exchanged pursuant to international tax treaties. The present lack of access to this data is an unquestionable handicap to effective oversight in a significant area. However, the Department of the Treasury and the Internal Revenue Service are presently pursuing possible administrative and diplomatic solutions. Due to the international sensitivity of the issues involved, we believe that, for the present, good faith diplomatic initiatives probably are the most appropriate and practical approach for obtaining access to tax treaty data.

As discussed previously, it is important that any amendment to 26 U.S.C. § 6103 retain the safeguards provided in the current law. GAO's experience has shown that these limitations and safeguards have not adversely affected its ability to effectively report its findings.

Chairman RANGEL. Thank you so much, gentlemen.

Commissioner Egger is with us from the Internal Revenue Service, and will be testifying on behalf of his Service, as well as the Treasury Department. It is always good to have you, Commissioner.

We thank you for your cooperation and look forward to continually working with you in carrying out your mandate and our congressional responsibilities.

STATEMENT OF ROSCOE L. EGGER, JR., COMMISSIONER OF INTERNAL REVENUE, ACCOMPANIED BY THOMAS J. CLANCY, DIRECTOR, CRIMINAL INVESTIGATION DIVISION, AND PETER V. FILPI, DIRECTOR, DISCLOSURE LITIGATION DIVISION

Mr. EGGER. Thank you, Mr. Chairman. It is always a pleasure to be here.

I am pleased to appear before you to discuss our experience with the disclosure provisions of Internal Revenue Code Section 6103. With me today are Thomas J. Clancy, Director, Criminal Investigation Division and Peter V. Filpi, Director, Disclosure Litigation Division.

As you know, ours is a self-assessment tax system that depends substantially on voluntary compliance by taxpayers. The Secretary of the Treasury has broad authority to require all taxpayers to file tax returns and keep records necessary to a determination of their tax liability.[1] In addition, the Secretary is authorized to examine books, papers, records, or other data relevant or material to the determination of the tax liability.[2] These powers are essential to enable the Internal Revenue Service to obtain by administrative action information necessary for tax administration.

The scope and complexity of the tax laws require the Service to make a broad range of inquiries of taxpayers, both on the returns they file and during examinations and investigations. Last year, we received more than 143 million returns from taxpayers, and conducted more than 2.1 million examinations. We also initiated more than 7,100 criminal investigations. As a consequence, the Service probably has more information concerning the lives and affairs of individuals and others than any other agency of the Federal Government.

---

[1] Section 6001 of the Internal Revenue Code. (Unless otherwise specified, all references are to the Internal Revenue Code of 1954, as amended.)

[2] Section 7602.

There is little wonder then that Federal law enforcement agencies find IRS an attractive partner in conducting investigations. Prior to the enactment of the Tax Reform Act [TRA] of 1976, the information flow between IRS and other Federal agencies was handled in a fairly routine manner. Tax returns were described by statute as "public information", and generally were open to inspection by other Federal agencies under Presidential Executive Order and implementing regulations approved by the President. They were made available to the Department of Justice or to U.S. attorneys "when necessary in the performance of * * * official duties," and in civil cases where the United States was a party in interest. U.S. attorneys made direct requests to local IRS districts for copies of tax returns and other information.

Attention focused on the need for amending the tax disclosure statutes as a result of investigations concerning the use of tax information for nontax purposes during the mid-1970's. The public became concerned that tax returns were perhaps not the private documents many had thought. This proved compelling for Congress to decide that, after 40 years, the disclosure statutes needed revision. Several serious questions were raised during these deliberations:

One. Does the extent of actual and potential disclosure for nontax purposes conflict with the citizen's expectation of privacy for his/her personal financial information?

Two. To what extent does the public's reaction to potential abuse of privacy impair the effectiveness of our country's voluntary tax assessment system?

Three. Should tax returns and tax information be used for any purpose other than tax administration?

Congress attempted in the TRA of 1976 to balance the individual's expectations of fairness and privacy with the legitimate needs of other Federal agencies. The Congress decided that tax returns and tax information should generally be treated as confidential, and that disclosure would be authorized for specifically authorized purposes subject to procedural safeguards. It also decided that prior law and regulations did not afford individuals an appropriate degree of privacy protection for tax returns. As a result, Internal Revenue Code section 6103 was amended.

Section 6103 permits disclosures of tax information for Federal nontax criminal law enforcement purposes, subject to certain safeguards, but generally does not permit such disclosures for Federal nontax civil enforcement purposes, and permits no disclosures for State nontax criminal or civil enforcement purposes.

With respect to disclosures for nontax criminal law enforcement, section 6103 creates a distinction between returns filed by taxpayers (returns) and information furnished to the Service by the taxpayer or his representative (taxpayer return information), on the one hand, and information from sources other than the taxpayer (return information other than taxpayer return information) on the other. In the case of returns and taxpayer return information, the Department of Justice (DOJ) and other Federal agencies must obtain a court order to obtain this information for nontax criminal law enforcement purposes. To obtain the order, the Department or other Federal agency must show that there is reason to believe that a specific criminal act has been committed, that there is reason to believe that the information sought is probative evidence of a matter in issue, and that the information sought cannot be reasonably obtained elsewhere unless such tax information constitutes the most probative evidence.

In the case of information obtained by the Service from third parties, disclosure is permitted to personnel of other Federal agencies upon written request from the head of the agency, or, in the case of DOJ, the Attorney General, the Deputy Attorney General, or an Assistant Attorney General. The written request must set forth certain specific information, including the specific reasons why the disclosure is or may be material to the nontax criminal proceeding or investigation. In addition, the Internal Revenue Service is authorized to volunteer third party evidence of a possible violation of a nontax related Federal criminal law to the head of the agency charged with enforcing that law.

The Service has been mindful of the potential for problems with 6103 as it has taken steps to implement it. Procedures covering disclosures for nontax criminal prosecution or investigation were coordinated with the Criminal Division of the Department of Justice, and the Service assisted in the preparation of a manual for U.S. attorneys for their guidance in obtaining returns and return information. We have trained our employees and created disclosure officer positions in each district, region, and service center to administer disclosure activities.

We have also undertaken numerous administrative changes which have streamlined the disclosure process. In particular, we have decentralized the approval and processing procedures for disclosure in order to be more responsive to requests for returns and return information. I have attached to my statement a summary listing the actions the Service has taken to decentralize.

In addition to decentralizing, the Service has promoted the use of section 6103(i)(3) provisions for disclosing nontax criminal violations. A series of memoranda to the field, as well as revised manual procedures, have been issued which explain and encourage the proper use of section 6103(i)(3). This activity culminated in a January 1981 memorandum to all regional commissioners requesting a response within 45 days to the assistant commissioner (compliance) outlining the steps that "have or will be taken to foster compliance with section 6103(i)(3)." Analysis of the responses to this request identified additional matters which required clarification. Changes to our manual guidelines reflecting these clarifications are being made.

We have also revised grand jury approval procedures to improve our capability for cooperation with other law enforcement agencies in joint criminal investigations. Our inventory of such cases has more than doubled over the past year. This is due in part to the improved approval process for such investigations, which has reduced substantially the time for obtaining approval.

This has been accomplished by establishing time frames for each level of managerial approval of the request—10 workdays for the chief of the district's criminal investigation division, 5 workdays for the district director, 5 workdays for the regional commissioner, and 10 workdays for the regional counsel. Approval authority for grand jury requests was delegated to our regional commissioners, and they may redelegate that authority to the assistant regional commissioners (criminal investigation). These approvals must receive the concurrence of the regional counsel. Expansions of existing grand jury authorizations now may be approved by district directors with the concurrence of the deputy regional counsel (criminal tax). We currently are considering additional revisions that would further enhance our participation in these proceedings.

The Service's efforts to insure cooperation with the law enforcement agencies at Justice have resulted in the establishment in May 1980, of the IRS "hot line" and the IRS-DOJ coordinating committee. The "hot line" functions as follows: Whenever any DOJ division or bureau such as the Tax Division, FBI, DEA, or U.S. attorney feels that they have a 6103 problem, they are to contact the Office of Legal Support Services, Department of Justice, Washington, D.C. That office will then contact IRS. Problems will be resolved on a priority basis. While I should note that we believe this procedure to be viable, the number of times it has been used is not substantial.

The IRS-DOJ coordinating committee was created to resolve immediate section 6103 concerns, but it ultimately focused on procedures and strategies for the long-term resolution of problems. The committee was made up of representatives from the Department of Justice Criminal Division, Tax Division, and Office of Legal Support Services and representatives from the IRS Disclosure Operations Division and Disclosure Litigation Division.

The committee met from May through September 1980, but has not met since. Recent contacts with the Director, Office of Legal Support Services, DOJ, indicate that while the Department of Justice still wishes to continue the coordinating committee, it feels the meetings should be held only when either side feels a need to convene the committee.

Notwithstanding our attempts to improve efficiency in working with the disclosure provisions, the information flow between IRS and other Federal agencies is certainly less now than it was prior to the TRA of 1976. For example, in 1975 there were 1,750 DOJ requests authorized involving over 6,800 taxpayers compared to 291 requests involving approximately 1,200 taxpayers in 1980.[1]

The Service's participation in Strike Force cases has also declined from 616 in inventory for fiscal year 1976 to 284 in 1980. This is due at least in part to the more strict disclosure provisions of 6103. Strike force attorneys have observed that the open and frank discussions concerning strike force investigations which used to take place with IRS personnel no longer occur. While 6103 permits IRS to disclose tax information to the Department of Justice in the course of tax or joint tax/nontax criminal cases, IRS is prohibited from sharing such information with the Department of Justice outside the 6103(i) procedures in purely nontax criminal cases. Informally, strike force attorneys have also indicated that they did not want to contend with the administrative paperwork associated with 6103.

---

[1] It should be recognized that certain differences in definition exist for our data on 6103 requests pre vs. post the TRA of 1976 and, therefore, such data is not strictly comparable.

The complexities of the law have created some problems for our field agents. Each new assignment, whether a task force, grand jury or strike force investigation, requires an understanding of differing rules.

An even more difficult problem occurs when IRS agents, acting in what they believe to be a lawful manner are sued for violations of the disclosure laws. Recent cases against agents in Federal courts in South Carolina and Colorado involved situations that for years prior to the TRA of 1976 were considered sound investigative techniques. Even though the case in South Carolina was resolved in favor of the agents, the Service's investigative technique was found contrary to 6103. We are appealing the case in Colorado. Our employees have gotten the message that their actions are subject to scrutiny. While these employees must, of course, operate within the law, the fear of prosecution and civil damages for innocent error is, to some extent, inhibiting.

The Service compiles statistics covering the frequency and type of requests for information it receives under section 6103. A review of this information suggests that the provisions of the existing statute have apparently been underutilized. At the same time, the Service's turnaround time after official receipt of such requests has generally been timely, running about 6 days absent extraordinary circumstances.

In addition, the law enforcement community has expressed its difficulty in dealing with certain of the definitions in section 6103. As I believe the Deputy Attorney General has testified, the Justice Department has found this definitional structure to be complicated and difficult to apply. The effect of the definitions is to provide statutory protection analogous to—but less stringent than—search warrant procedures. It is, of course, essential that our self-assessment tax system remain unimpaired. A cornerstone of the voluntary compliance system is assurance to taxpayers that the returns which the Internal Revenue Code requires them to file and the supporting books and records which the code requires them to keep are not readily available for nontax criminal investigations without appropriate safeguards, such as the court supervision provided by present law.

We have experienced our share of problems with 6103, but frankly the situation may be improving somewhat. Our most recent experience has shown that we are learning to work with the provisions of the disclosure statute, and I am hopeful that the effects of our efforts to streamline the system are starting to pay off. For example, the IRS strike force case inventory is up somewhat in 1981. Also, there has been an increase in the volume of requests by U.S. attorneys made during the first 9 months of 1981, although this growth is primarily in offices that have been active in making requests in the past.

What I hope this shows is that we have taken appropriate initiatives for change in our 6103 procedures from an administration standpoint. At the same time, certain legislative action is necessary. The administration bill to amend section 6103, S. 1891, strikes the proper balance between protection of our self-assessment tax system and enhancing nontax related criminal law enforcement efforts. It retains the court order requirement for disclosure of all tax returns and information obtained from individual taxpayers and from very small other taxpayer entities such as one or two member corporations and partnerships. Further, the Service could volunteer to DOJ evidence of possible nontax Federal criminal violations taken from the books and records of a corporation or partnership entity only if we determined that the entity had been formed or was being used for criminal purposes. I think you will agree in the case of criminal entities, there is no policy reason to afford them the privacy protection which the internal revenue laws provide to other taxpayers.

The administration bill also has the effect of decentralizing from the Washington offices of the Department of Justice to responsible law enforcement officials in the field the authority to request information—thus significantly improving the timeliness and responsiveness of such requests. Further, it would correct a problem in the existing statute which can have the effect of requiring law enforcement officials to know in advance the contents of taxpayer return information before making a request for disclosure.

Mr. Chairman, this concludes my prepared statement. I would be glad to respond to any questions which you or members of your subcommittee may have.

[An attachment to the prepared statement follows:]

Actions Taken in Decentralization of IRC 6103(i) (1), (2) and (3) Disclosures

The following is a list of actions that have been taken to decentralize disclosures under IRC 6103(i) (1), (2) and (3):

1. *Revised delegation order:* A Delegation Order was issued effective June 1, 1980, giving authority to District Directors and Assistant District Directors to make disclosure directly to the Department of Justice (DOJ) and the heads of Federal agencies under IRC 6103(i) (1) and (2). Authority was also delegated to Regional Commissioners to make disclosures of posssible violations of Federal nontax criminal statutes under IRC 6103(i)(3). On May 26, 1981, District and Service Center Directors and their Assistants were delegated authority to make disclosures under IRC 6103(i)(3).

2. *Revised IRS manual:* Chapter (28)00 of Internal Revenue Manual 1272, Disclosure of official Information Handbook, has been revised and issued to the field. Significant changes in this manual procedure are as follows:

(*a*) IRS liaison districts were designated specific responsibility for coordinating with U.S. Attorneys and other DOJ agencies.

(*b*) Specific time frames were established for completing processing for both routine and emergency requests. We have established the requirement that Distict, Regional, and National Office officials become personally involved when the request is not filled with the specified time frames.

(*c*) A checklist was developed for use by District Disclosure personnel to insure through reviewing and processing of ex parte court orders and written requests without delay. In addition, a decision model chart was included in the chapter as a guide for processing.

(*d*) Instructions were included in the text for processing special requests from DOJ.

(*e*) Detailed instructions were provided for the processing of ex parte court orders under IRC 6103(i)(1) and written requests from heads of Federal agencies under IRC 61030(i)(2).

(*f*) The District Director was identified as the IRS official with primary responsibility for liaison with U.S. attorneys.

(*g*) New instructions were included to provide for the disclosure of evidence of violations of Federal nontax criminal laws.

(*h*) Instructions concerning referrals to the Strike Force, DOJ, are changed to require that the Region, instead of the National Office, make such referrals.

3. *Training of disclosure personnel:* Regional Disclosure Officers received training in the new procedures by May 1980. They subsequently returned to their areas and conducted similar training for Disclosure Officers and Specialists from each district.

4. *Coordination with DOJ:* A meeting was held with the Acting Director, Office of Legal Support Services, DOJ and a representative of the Executive Office of United States Attorneys on April 23, 1980, and our decentralization plan was explained. Subsequently, we have held several meetings with officials in the Office of Legal Support Services and they have received training about our new procedures.

5. *"Hot Line" established:* A "hot line" has been established between Disclosure Operations Division and DOJ to handle problems arising during the first 2-3 weeks of our decentralization.

6. *Priority requests to FRCS:* The IRS Facilities Managment Division, which is responsible for coordination with Federal Records Centers (FRCs), has agreed to identify IRC 6103(i)(1) and (i)(2) requests as priority to FRCs.

7. *Development of video training tape:* In participation with the Tax and Criminal Divisions, DOJ, we have developed a training video tape which is designed to stimulate more referrals to DOJ under IRC 6103(i)(3). This tape is currently being shown to IRS field personnel.

8. *IRS-DOJ Coordinating Committee:* We have established an IRS-DOJ Coordinating Committee. The Directors, Disclosure Operations Divison and Disclosure Litigation Divison are designated as IRS representatives. This committee has met several times during the past months and will continue to exchange information and maintain a high level of cooperation between agencies.

9. *Briefing U.S. attorneys:* Each District Office made contact with their U.S. Attorney(s) office for the purpose of offering to brief them concerning the new procedures.

10. *Monitoring IRS response:* During the balance of fiscal year 1980 we visited IRS offices in three of seven Regions that receive the largest number of IRC 6103(i) (1) and (2) requests. The remaining four Regions were visited during the fiscal year 1981.

Chairman RANGEL. Thank you, sir.

Mr. Pickle.

Mr. PICKLE. Thank you, Mr. Chairman.

Mr. Egger, I notice on page 7 you relate that the IRS effort to insure the cooperation of the law enforcement agencies has resulted in establishment of this hot line, and you tell us how it works and functions.

Then you conclude that, "While I should note we believe this procedure to be viable, the number of times it has been used is not substantial."

Why is it not substantial, if it is a viable procedure and a workable procedure, and yet has not been used, why has it not been used?

Mr. EGGER. I would like Mr. Filpi to answer that question.

Mr. FILPI. The hot line has been used in the early stages of the 1976 Tax Reform Act when there was some confusion.

As time went on, the U.S. attorneys became familiar with 6103. If they had problems, they would call Department of Justice directly and contact us.

The Department of Justice attorneys that were supporting U.S. attorneys have now become familiar with the act and the only time they call us is when they have a real problem and when they do, we expedite that request in a manner to satisfy both departments.

CRIMINAL PENALTY PROVISION: COMPARISON OF 26 U.S.C. §7213, H.R. 1502 AND THE ADMINISTRATION'S PROPOSAL

26 U.S.C. §7213	H.R. 1502 and ADMINISTRATION'S PROPOSAL
Provides criminal penalties for unauthorized disclosure of tax information.	Adds an affirmative defense to a prosecution under this section: i.e., that the disclosure resulted from a good faith but erroneous interpretation of the law.

GAO Comments

Enactment of the proposed amendment would make clear that criminal sanctions attach only in the case of intentional violations of the disclosure provisions.

CIVIL PENALTY PROVISION: COMPARISON OF 26 U.S.C. §7217, H.R. 1502 AND THE ADMINISTRATION'S PROPOSAL

26 U.S.C. §7217	H.R. 1502 and ADMINISTRATION'S PROPOSAL
Authorizes the payment of civil damages to a taxpayer by the individual responsible for unauthorized disclosures of tax information.	When unauthorized disclosure is made by Federal employee, the Government, rather than the individual employee, is responsible for payment of civil damages.

GAO Comments

The Government would be civilly liable under the proposed amendment for all unauthorized disclosures made by Federal employees, including those made intentionally and with knowledge of the disclosure restrictions. However, this would not affect the Government's ability to proceed criminally against employees who intentionally violate section 6103.

Mr. PICKLE. Well, you continue along this line and then on page 11 you say that you are "hopeful that the effects of our efforts to streamline the system are starting to pay off."

Then you give an example. Why are they beginning to pay off now when we have not changed the law any?

Mr. EGGER. We have gone a long way, Mr. Pickle, in decentralizing the authority to make certain disclosures. We believe not only the members of our staff but the Department of Justice is finding it more comfortable to work with some of the complex definitional problems. For example, in this fiscal year, 1981 I think in 9 months we literally doubled the number of disclosures made under section 6103(i)(3) and the number of requests from U.S. attorneys for information on tax returns are increasing.

Mr. PICKLE. Well, it just seems to me you are a bit inconsistent. You point out that you have the hot line and nobody uses it. You regret it. On the other hand, you said, though, that the IRS strike force case inventory has picked up somewhat in 1981. So the disclosure statute is being used, but not being used very much. Is it?

Mr. EGGER. About half of the requests from the U.S. attorneys are coming from 10 of the jurisdictions.

Mr. PICKLE. The same jurisdictions?

Mr. EGGER. Yes, sir.

Mr. PICKLE. Were you here when the GAO official testified?

Mr. EGGER. Yes, sir.

Mr. PICKLE. They made some specific suggestions. Did you think that those suggestions were reasonable or do you differ with them?

Mr. EGGER. I think those suggestions on balance tend to be pretty parallel with the administration bill here.

Mr. PICKLE. Do we have an administration bill?

Chairman RANGEL. Yes, it is a Senate bill.

Mr. PICKLE. Yes, that's right; thank you. But I'm told there is no House companion bill to S. 1891. The only House bill, I presume, is that which was introduced by Congressman Gibbons. It is similar to Senator Nunn's bill, S. 732.

Mr. EGGER. Yes, sir, that is correct. I just was reminded that the primary use of the hot line is to address specific problems related to Department of Justice requests for access to returns or return information. We do not know why the Department of Justice has not used the procedure more often.

Mr. PICKLE. Thank you, Mr. Chairman.

Mr. RANGEL. Mr. Crane?

Mr. CRANE. Thank you, Mr. Chairman. I would like to welcome the Commissioner before the committee.

Commissioner Egger, since January 1, 1977, the effective date of section 6103, how many times has the IRS had to go to Federal court to enforce a third party suit?

Mr. EGGER. I'm not sure I can give you the details. I can furnish it for the record but it's been a lot.

Mr. CRANE. And do you know how many times in the calendar year 1980?

Mr. EGGER. I'm afraid I can't give you the number of times but we run into it with the tax protesters constantly.

[The following was subsequently received:]

ENFORCEMENT ACTIONS IN THIRD PARTY RECORDKEEPER SUMMONS CASES (IRC SECTION 7609)

The following infomation is taken from a computer printout dated October 29, 1981 on closed cases only. We do not have this data for cases which are still open.

Fiscal year 1980:	
Enforcement petitions filed in Federal court	798
Withdrawn prior to court action	87
Won	702
Partial win	5
Lost	4
Fiscal year 1981:	
Enforcement petitions filed in Federal court	152
Withdrawn prior to court action	7
Won	145
Lost	0

We do not have complete data on the reasons for the withdrawn cases. The partial data we do have is for 1980 and shows the following reasons:

Stay withdrawn and recordkeeper complied	53
Records provided by summoned party (nonstay or exception cases)	12
Records provided by another source	3
Case closed	2
Information not relevant	1
Incorrect dates in caption	2
Other	1

The above charts reflect all petitions filed in Section 7609 cases. The following charts exclude cases in which court action would have been required in spite of Section 7609.

Fiscal year 1980:	
Enforcement petitions filed in Federal court	735
Withdrawn prior to court action	74
Won	652
Partial win	5
Lost	4
Fiscal year 1981:	
Enforcement petitions filed in Federal court	143
Withdrawn prior to court action	4
Won	139
Lost	0

For fiscal year 1980, the reasons for withdrawal are the same as above except that the second category "Records provided by summoned party" would be excluded.

Mr. CRANE. How many times have you lost in court in say, calendar year 1980?

Mr. EGGER. To the best of my knowledge, none.

Mr. CRANE. How many negligence suits have been brought against IRS personnel since they have been personally liable under the code?

[The following was subsequently received from Mr. Egger:]

Since the Tax Reform Act of 1976, 21 suits have been filed against IRS employees pursuant to IRC Section 7217. As of June 30, 1981, 14 of those suits have been dismissed in favor of the agents, including the *Calhoun* case. Six suits are currently pending in various district courts. We are currently appealing the decision in the *Rodgers* case.

Mr. CRANE. And did that involve any personnal expense by the IRS employees in those suits?

Mr. EGGER. I believe the law permits us to assume that responsibility for the individuals, but their time must be devoted to participation in those proceedings.

Mr. CRANE. Can you estimate what will be the cost to IRS and its personnel if it is required to divulge tax information to other law enforcement agencies?

Mr. EGGER. I really don't think we have developed any cost figures on that. It should not be terribly significant, though.

Mr. CRANE. I assume there will be increased budgetary requirements. Have you any estimate as to the impact, the dollar impact on these additional burdens that you would be assuming if this legislation passes?

Mr. EGGER. I do not have an estimate with me, Mr. Crane. We will be happy to check into it and if we have such information it will be in the record.

[The following was subsequently received:]

We have undertaken a review of the budget impact for IRS under the proposed change to IRC section 6103(i)(3) and find that no additional resources will be necessary to meet our responsibilities.

Mr. CRANE. Thank you.

Do you think that the enactment of any of these bills is apt to have any impact or affect on our system of voluntary compliance?

Mr. EGGER. I really don't think so. My personal belief is that the American public is not very sympathetic with criminal activity and in each instance here the involvement is with people engaged in that kind of activity. I do not think that the provisions of the law as such, particularly where returns themselves are subject to court review before they can be transmitted even under any of these versions, will have any major impact or any significant impact on the self-assessment system.

Mr. CRANE. Well, you could, theoretically at least, have a case where you had determined there had been a violation of the Tax Code but you also passed information on to Justice that caused Justice to investigate, to prosecute and maybe lose. And that is what I'm thinking about in terms of what impact that might have in terms of voluntary compliance if there were any significant number of cases where the information that was relinquished to Justice in the pursuit of your objectives, or services resulted in what might be perceived by taxpayers as harassment.

Mr. EGGER. The only instances of that, again, are in those who seem bent on the violation of the tax laws anyway and they use that kind of an argument publicly and otherwise to accuse us of harassment, when in fact in most of the cases I have come across it is simply a question of proper investigative techniques and things which we should be doing.

Mr. CRANE. Do you anticipate any fifth amendment problems that will beset you in regard to the exchange of tax information called for in these bills?

Mr. EGGER. I can't say it's not going to happen because we do know that in one or two instances in court cases, the lower courts at least have held that where taxpayers honestly believed that they were violating their fifth amendment rights that it became a problem. Now, how far that is going to go, I believe it is just impossible at this time to tell.

I'm assured by counsel, at least at the moment, that it is not a terribly significant problem. I cannot say that it could not be a problem in the future.

Mr. CRANE. When we heard testimony earlier today, one of the objections to the bill came from former Commissioner Kurtz and he indicated that the IRS, when it makes a recommendation under the provisions of this bill to the Justice Department for prosecution of a tax crime, that all information gathered by the Service, whether relevant or not to the criminal tax referral, would be sent to Justice and that they, in turn, then would be free to use such information in nontax criminal cases.

And it seems to me that that is kind of a Pandora's box with regard to the fifth amendment and voluntary compliance. Don't you think, realistically there would be a growing concern on the part of taxpayers about what they release to you on tax-related matters because of the realization that anything that was background information in the development of your objective was immediately going to be passed on to Justice to use in any way they wanted to use it?

Mr. EGGER. Well, as I said before, we have reviewed that particular point with counsel and at this point we do not believe that would be a significant problem, but a lot would depend on how the courts view that situation in the future as cases arise.

Mr. CRANE. I mean, I am just wondering, if you were the individual involved, how do you redress that kind of grievance if, in fact, it does develop? I mean even in a single case? What protection is there for the individual citizen? That information has already been divulged with his expectation that it was going to remain confidential with you?

Mr. EGGER. Except that if the disclosure laws change, he no longer has that expectation. He will know that on the return, any information that he discloses is apt to be referred to the Department of Justice or to another agency.

Mr. CRANE. And you don't think that is going to have any impact on voluntary compliance?

Mr. EGGER. As I said before, I really don't think so. I think most people believe, even under current law that if they put on tax returns evidence of criminal activity, that it is more than likely that that information will become known to other agencies.

Mr. CRANE. Well, then, if they are not putting that evidence into their tax form, I think that kind of negates Senator Nunn's argument as to the necessity of the legislation. If they have already lied to you and they have withheld information from you and your people's training and function is exclusively to get at tax-related illegalities, if you acquired something else in the process of that kind of investigation, presumably your people would not be trained to know whether they spotted an illegality or not in a non-tax-related matter; is not that so?

Mr. EGGER. Well, what usually happens is that the information that is required in the return in terms of income disclosures and so on, assuming they do not choose to violate the tax laws, is obfuscated or clouded in some fashion so as not to be clear that it is from nontax criminal sources. And typically, that information is developed in the course of investigations of our own. So it is that kind of thing, I believe, that is concerning the Department of Justice with respect to the ability to transmit that kind of information.

Mr. CRANE. Thank you, sir. I have no further questions.

Chairman RANGEL. Mr. Moore.

Mr. MOORE. Thank you, Mr. Chairman.

Mr. Commissioner, I appreciate your being here and the spirit of cooperation in your testimony lends to what some of us believe is a problem we can rectify. The other former commissioners made statements that I was not able to question them on due to having to go to a vote, but I would like to ask you and I think you have already touched on it. And that was the fact that I think former Commissioner Kurtz made a comment on in his written testimony that there is a premise that someone will be honest with the IRS and dishonest with other agencies or that they are aware of this law and will put things in there that would convict them of a crime, knowing you can't turn it over to another agency.

I think, as you indicated in your answer to that question to me, that that is a very specious argument. It seems to me that someone who has been engaged in any kind of shady activity would most likely suspect you would be furnishing over any evidence of that to another agency, and, therefore would be lying to the IRS just as they would to the SEC or the FTC or the FBI or anyone else.

Mr. EGGER. In general, I think that is correct. However, we have had instances of people disclosing illegal activities on returns and reporting the income. In that fashion I assume they were well aware that the law did not permit us to then voluntarily turn that information over to the Department of Justice for prosecution. It does not happen often, obviously, and I suspect that for the most part people engaged in illegal activity either do not report the income or if they do, as I said, it is confused or clouded in some fashion so it can't be readily discerned as the source.

Mr. MOORE. Do you have any opinion—and you may have answered this too, but do you think this would have a chilling or an enforcing effect on voluntary compliance of taxpayers in general? We heard your testimony earlier this morning about the problem we are having with the underground economy. If we were to make the amendments as you are testifying to and as the Justice Department is indicating, or something along the lines of S. 1891 as Senator Nunn testified to, do you think this would assist the taxpayers in being a bit more honest in reporting to the IRS or do you think it would have a chilling effect on their voluntary compliance?

Mr. EGGER. I don't think it will have a chilling effect because this bill does preserve the confidentiality of the tax return itself and the information which is supplied by certain taxpayers. It still requires a court order as it does under present law. My feeling is, however, that if people believe that criminals engaged in organized criminal activity, narcotics trafficking, and so on will be apprehended more readily, I think they will feel better about paying their taxes in general. I think they will feel better about the whole law enforcement effort.

Mr. MOORE. In my own district back home, I have run across examples of the underground economy with people not recording cash income and in fact doing business on a cash basis. What is your opinion about those kinds of people once they learn that Congress has changed the rules to make it easier for general enforcement of the laws of this country? Do you think they are liable to be impressed by the general enforcement possibly catching them in some way or do you think they would ignore those changes?

Mr. EGGER. I strongly suspect that this bill will not have much effect on that. However, there are other things which I believe can be done which would have much more of an effect on the reporting of that kind of income and probably discouraging people from leaving it off the returns. I am talking about information reporting of all sorts, things of that kind, where taxpayers believe that the IRS has the capability of discovering that kind of unreported income.

Mr. MOORE. Do you think there would be an increased flow to your Service from other law enforcement agencies if we, in fact, passed a bill something like S. 1891 which would increase the flow of information from your Service to those agencies?

Mr. EGGER. Certainly our hope is that our ability to work more closely with other enforcement agencies will be a two-way street, in that in working together on joint nontax criminal investigations the flow of information from them will be very positive. We have learned that in south Florida, for example, in connection with some of the drug traffic investigations in which we participate.

Mr. MOORE. The two questions I just asked lead me to this situation. I have just learned in my district of where some subcontractors very often will take a cash payment from a general contractor and not report that as income. It is possible, it appears to me, that the Department of Labor or Social Security Administration will eventually uncover some of that by virtue of following up on complaints by employees to a subcontractor that their returns are not paid or they may have been paid for their contributions and that might eventually flow back to you which would help you, in turn, get to the subcontractor who never made the disclosure of the income to start with.

That is what I was aiming at in getting at these questions.

Mr. EGGER. Exactly. And we think we have only scratched the surface on the kind and combinations of information which can be put together and processed with up-to-date technology and which will permit us to discover a great deal more of that type of activity than we have been able to do in the past.

Mr. MOORE. Lastly, Mr. Commissioner and Mr. Chairman, there is a Library of Congress study out that staff has supplied me that discusses some of the concerns with S. 1891 and points out amendments to tighten it up and calms some of these concerns somewhat more satisfactorily.

I think that it is entirely possible that a bill like S. 1891 could be amended to still make it an improvement over existing law, but still satisfy some of the valid concerns. However, Mr. Commissioner, again, I thank you for your spirit of cooperation. The last time we had you before our Oversight Committee there was to be a bill forthcoming from the administration on ways of getting at the underground economy and reporting. I don't know if that bill has been sent to us yet. I have not seen it and I look forward, sincerely, to receiving it as soon as possible. I'm seeing it now in my own district and know that it, in fact, is taking place, and, it is putting honest subcontractors out of business as he no longer can bid for the contract because he is higher than the one who is not reporting the income.

Mr. EGGER. I assume you let the IRS know about that.

Mr. MOORE. Well, I have encouraged this fellow to contact the local IRS to report the examples wherein he knows his competitiors are taking cash contracts and not reporting it. In any event, maybe this will help in some small part.

Chairman RANGEL. Mr. Duncan?

Mr. DUNCAN. Thank you, Mr. Chairman.

Mr. Commissioner, this morning we had some testimony on information that was used in disclosure statements from a panel from the Justice Department. Do you look with favor upon such information?

Mr. EGGER. I'm unaware of anything of that sort. If the suggestion is to improper actions, that suggestion has been made to me in a letter which I very promptly turned over to the Department of Treasury for investigation.

Mr. DUNCAN. Has such information been denied or such requests been denied?

Mr. EGGER. We have not dealt with it. We have turned it over to the Inspector General to make an independent investigation.

Mr. DUNCAN. How many such requests do you have pending?

Mr. EGGER. One.

Mr. DUNCAN. How many disclosures were made by the IRS for the last year pursuant to written request?

Mr. EGGER. We have that information here. Mr. Clancy has it right here.

Why don't you go ahead and read it off to him.

Mr. CLANCY. The Tax Reform Act starting in January of 1977.

Mr. DUNCAN. Do you have it for each year since then?

Mr. CLANCY. Yes, sir.

In fiscal year 1981, the total section 6103(i)(1) requests were 38 and the (i)(2) requests were 35.

Mr. EGGER. Section 6103(i)(1) requests, Mr. Duncan, are for returns and taxpayer return information.

Mr. DUNCAN. It would appear that you would need a lot of manpower to comply with that.

Mr. CLANCY. I would like to correct that, Mr. Congressman. I gave you a subtotal. The total for all of the U.S. attorneys offices for the period from January 1, 1980, to September 30, 1981, were 203(i)(1) requests and 177(i)(2) requests.

Mr. DUNCAN. How many of the requests you provided were related to drug trafficking and organized crime?

Mr. EGGER. We don't have that broken down here. I'll check and if we can make it available we will put it in the record, Mr. Duncan.

[The following was subsequently received:]

Requests for information under IRC Section 6103 (i)(1) and (i)(2) are not required to identify that drug trafficking or organized crime is involved, and the service, therefore, has no statistics on this. A review of our records does reflect, however, that in 1978, the Service responded to 88 requests under IRC 6103 (i)(1) and (i)(2) from the Criminal Division of the Department of Justice that appear to be related to such crime figures. In addition, for the period of January 1, 1980, through September 30, 1981, the Service processed 67 requests from Strike Force Attorneys, whose requests generally involve organized crime matters.

Mr. DUNCAN. Thank you, Mr. Chairman.

Chairman RANGEL. I'd like to pursue that line of questioning, Mr. Duncan. The IRS has been pictured as an agency that could assist in the indictment and conviction of all of the criminals that seem to be slipping through the system. And while I recognize that you like IRS to be perceived as the tax collection agency of the country, still your testimony indicates that you are quite proud of the cooperation that you have given to law enforcement agencies. So, Mr. Egger, it would help to know exactly what is related to drug trafficking and organized crime. Obviously this is what all of the critics of IRS are talking about, that you are allowing these big international drug traffickers to get away because you are not cooperating with DEA or Justice. So, how many requests deal with this subject and how many have you turned down?

Mr. EGGER. Mr. Chairman, these are requests of tax information for nontax criminal purposes, if you are talking about IRS's cooperation with other agencies in the investigation of drug dealers.

Chairman RANGEL. I must have misunderstood Mr. Duncan's question. I thought he asked how many of these requests were related to drug trafficking and organized crime.

Mr. CLANCY. That was his question, but it was under the section 6103(i) provisions that allows the Justice Department to request the information for nontax criminal purposes. We furnish that information to them. If they wish us to join in a joint investigation, they don't follow together, if you follow what I'm saying. We work a good deal with the Department of Justice in joint investigations. A high percentage of them are within the grand jury, joint grand jury investigations with other agencies.

Mr. EGGER. Perhaps I can clear this up just a little bit. We have two programs, our special enforcement program, which is drug trafficking, organized crime, et cetera, and the general enforcement program, which is just the tax crimes by themselves. And something approaching 45 percent of our direct investigative expenditure of manpower is in the special program. So we have stepped up over the last 2½ or 3 years by a considerable amount the resources that are going into the investigation, either jointly with other agencies or by ourselves, of organized crime and drug trafficking and so on. We have more agents in south Florida dealing in these investigations than any other agency in the Federal Government.

Chairman RANGEL. Well, Commissioner, do you have the situation where DEA says that we know these drug traffickers and we don't have any evidence and we can't convict them and so we would like for you to check it out?

Mr. EGGER. We usually do that at the request of the Department of Treasury, Assistant Secretary for Enforcement.

Chairman RANGEL. The request would come from DEA?

Mr. EGGER. And Customs, yes, sir.

Chairman RANGEL. How many of those requests do you get? How many are denied? I'm trying to find out whether or not you are being cooperative and I need data. Obviously you can't do it unless you have requests. If they don't ask you, you can't do it.

Mr. EGGER. None of them are denied. In 1980, the Service made 2,179 disclosures for returns and return information under IRC 6103 (i)(1) and (i)(2) to the Department of Justice and other Federal agencies. We are unable to get to all of them immediately, of course, but the only ones that we turn down are sometimes matters that are referred to us and we discover upon initial investigation that there is no possibility of the existence of any such data in our files. Perhaps the individual is already in jail or something else has happened.

Chairman RANGEL. Let's put it this way, Mr. Clancy. Before we start examining how we should change the law in order to give law enforcement agencies more access to information that is acquired by or submitted to IRS, it would be very helpful to get some statistical data indicating what Mr. Duncan is referring to, and that is what requests are being made, and what type of information is voluntarily given by the IRS.

I don't want to get involved in the question of mandating the agents to turn over the criminal information, but I assume you have some data as to what type of crimes or alleged crimes routinely come across the agency's desk, and what the procedure is when that happens. I don't want to make you a nontax law enforcement agency, but I do want to see if you operate fully within the bounds of existing law. So, I want to get a better handle, statistically, as to what you call cooperation, because what we hear from proponents of drastic change in the law is lack of cooperation. And I think, Mr. Clancy, you could help us a great deal on that. I would ask that the record remain open so that if committee members and staff would like to acquire additional information, we could.

And specifically, you promised for the record, Mr. Commissioner, how many agents you think you would need to follow out the thrust of the Nunn bill. You don't have any problem with determining how many agents you will need, notwithstanding the problems with OMB. I mean, we could get the information, couldn't we?

Mr. EGGER. No. I promised Mr. Crane that we would look into that but I would like to elaborate that the thrust of this bill is not so much our lack of cooperation as it is making it easier for the Department of Justice attorneys and the U.S. attorneys to get information that is in our files.

Right now, I think the main complaint is that the procedures and the standards for obtaining that information are so restricted that it is hard to get at.

Chairman RANGEL. Well, there is a part of the bill which, as I understand it would change current law by which IRS agents are now authorized to turn over the information, and mandate that the agents do it. And that would mean that next time you testify before a congressional committee we would want to know whether you have carried out the mandate and turned it over. And to me it would seem that in order to do that, you would have to get special people who are experts in identifying these type of nontax crimes as opposed to just collecting the taxes and looking for tax violations. And that is what I am asking. If you carry out the provisions of the Nunn proposal, whether you support the bill or not, I would like to know what the cost would be.

Mr. EGGER. All right. We will provide something.

[The following was subsequently received:]

The Service currently turns over to the Department of Justice third party return information that may indicate a violation of nontax Federal criminal laws under

IRC 6103(i)(3). We do not foresee any increase in administrative costs resulting from the provisions of the Nunn bill which changes the disclosure authority from discretionary to mandatory.

Chairman RANGEL. Thank you very much.

We will again take a short recess and we will be sending some questions to the Service. Thank you.

We will recess and come back in 15 minutes and resume the hearing.

[Recess.]

Chairman RANGEL. The subcommittee will resume the hearing. There may be another interruption soon for another vote but we will try to continue on with the hearing.

We will be hearing from Owen Clarke, deputy commissioner, Commonwealth of Massachusetts, Department of Revenue, and from there we are going to a Justice Department witness who was scheduled earlier today.

Mr. Clarke, do you have a written statement?

STATEMENT OF OWEN L. CLARKE, DEPUTY COMMISSIONER, MULTISTATE, DEPARTMENT OF REVENUE, COMMONWEALTH OF MASSACHUSETTS

Mr. CLARKE. No, Mr. Chairman, because of the late notice that we received in Massachusetts, we have not submitted a prepared statement. We have a statement and we wish to be able to submit that statement at a later date.

Chairman RANGEL. Without objection, you may proceed.

Mr. CLARKE. Thank you very much. My name is Owen L. Clarke. I am Deputy Commissioner—Multistate, Department of Revenue, in Massachusetts. I'm past president of the National Association of Tax Administrators and was the president of that organization in 1976 when the Internal Revenue Code was last amended with respect to section 6103 and participated in discussions with several Federal agencies which at that time were involved in various proposals and recommendations then under consideration for amending section 6103.

As president of NATA and as Commissioner of Taxes in Massachusetts, I testified before the Ways and Means Committee of the House and subsequently before the appropriate Senate committees dealing with the whole question of the confidentiality of tax returns and tax return information, and with the important and very sensitive relations of the various State tax departments throughout the country and the Internal Revenue Service.

During that critical Watergate era, serious charges were raised, by some, that State tax department personnel were responsible for allowing unlawful and widespread disclosure of returns and/or information and that as a result thereof, the then existing exchange of information agreements, which practically all States had signed with the Internal Revenue Service, ought to be canceled and no further exchange of tax returns and/or information should be allowed.

The State tax administrators vigorously, and as subsequent amendment to section 6103 demonstrate, successfully proved that not one single instance in the so-called enemy list and not one single State tax return, or Federal return in the possession of any

State tax department, was found among the many thousands of returns discovered by Federal authorities in places where those returns were not supposed to be.

State tax authorities stated at that time, and they so state today, that the exchange agreements between the Internal Revenue Service and the States represent in all cases a most important part of State tax administration, and in some instances are an absolute requirement.

As a result of those meetings and on the testimony of State officials before the Congress, not only were the exchange of information agreements retained but they were, in fact, and with the active participation of the State administrators, strengthened and made more effective. The National Association of Tax Administrators, the national organization of all of the State tax departments, and individual State tax administrators have engaged in conferences and meetings with the Internal Revenue Service regularly since 1976, and on a frequent basis, to review and update these mutual assistance pacts.

Every State tax department has installed a system of guaranteeing that each of its employees is fully informed of all of the provisions contained, not only in the agreements, but also in each State tax law and of the penalties which are incurred by any employee who violates the confidentiality provisions. In Massachusetts all employees, including all new ones, are required to sign an affidavit stating that they have read and that they have an understanding of the confidentiality provisions of our law and of the mutual assistance pact. A copy of these documents is given to each employee to retain in his possession.

State tax administrators state unequivocally and without reservation that confidentiality of State tax returns and tax return information filed with them by their taxpayers is the very keystone of revenue production. Without confidentiality, or with a lack of respect by the taxpayers that the tax department really protects confidentiality, voluntary payment of taxes, which the entire system is built upon, will substantially diminish.

Every student and analyst of the American system of taxation comes to the same conclusion. Taxation experts from other countries repeat, over and over again, that the voluntary disclosure and payment of taxes by Americans is the most baffling phenomenon for them to understand, and they also conclude that the principle of confidentiality which exists between the taxpayer and the tax department is the foundation for such reporting and payment. But they carefully note that the American people are deeply convinced that when they file a tax return with a tax department that return will not show up next week as a gossip item at some cocktail party.

Both Federal and State tax administrators must at all cost make certain that this respect which the American taxpayers have for confidentiality is not destroyed or weakened. The taxpayers may rant and rave over the amount of taxes that they have to pay, "That rapacious tax collector has his hand in my pocket * * * or no matter how much I pay the Government still wants more * * * or if you open up your mouth in the tax collector's office he'll take the gold out of your teeth." But one statement that you do not hear from a taxpayer in this country is that his return can be, or is, revealed to every Tom, Dick, and Harry that comes along.

When, therefore, in 1976 the conflicting issues of privacy of information and the proper and necessary disclosure of information was presented to the Congress for resolution, at least in the field of tax administration, careful and proper result was effected by the amendments to section 6103. We think that the principle of confidentiality was totally understood by all parties at interest and that the principle would be made more secure by the provisions of section 6103 which were then, in fact, subsequently enacted into law.

When the discussions turned to the problem of using tax returns for evidence in matters not directly involving tax administration, or the violation of tax laws, there were strong representations made both by Federal and State tax administrators that under no circumstances should the returns of either tax agency ever be used except in directly related tax cases.

There was, however, the very important competing interest of those experts in the field of criminal justice who adequately convinced tax officials that a major injury to the public protection from crime could reasonably be expected to occur if a total prohibition against tax return use in a nontax criminal proceeding were to be enacted.

Now, this latter position became the prevailing one even though many State administrators were very reluctant to accept it.

The question then came, how should the confidentiality principle be breached and under what circumstances. Now, while this is a Federal law, and obviously Federal agencies involved played the major role in it, nevertheless section 6103 is directly and importantly related and tied to State tax administration.

Most State tax administrators thought—as indeed I thought, as one of their principal spokesmen at that time—that if any State tax returns were to be used in any nontax matter, that such return would be sought under the accepted principles and provisions set forth in section 6103 as then amended.

It was, and in my opinion still is, the State's position that no State tax administrator should willy-nilly refuse to allow a State tax return to be used in a nontax manner when a serious crime has been committed and the information on such State return is extremely important to and very substantive in proving such crime.

It is equally the State tax administrator's position that no public prosecutor should willy-nilly be allowed to use State tax returns in prosecution of nontax crimes simply because it would be of some aid and assistance to him to have such returns available.

The guidelines which were set forth for obtaining State tax returns, those three tests which have been discussed here in great detail today, were thought by us to be the ones which would be used exclusively if State tax returns were to be used in a nontax manner.

They are reasonable guidelines, and they were accepted by the States and the States thought they were going to be used.

However, State tax administrators generally, and of course the Massachusetts Tax Commissioner in particular, now know that the agreed upon guidelines are not the exclusive way for seeking State tax returns, at least up to the very unfortunate case against the Massachusetts Tax Commissioner.

In May of this year the U.S. Circuit Court of Appeals for the First Circuit in the matter of *L. Joyce Hampers* decided an appeal from the U.S. District Court in Boston which held the Commissioner in contempt for failure to surrender certain State tax returns in an arson case.

The circuit court, as you know—and I am sure this matter is in your files—reversed the lower court, and ordered the case remanded back to the lower court to, in fact, proceed to obtain the State tax returns sought under the provisions of the guidelines of 6103.

Obviously, Massachusetts considers confidentiality of the utmost importance even to the unhappy possibility of the imposition of a jail sentence to protect it. But the observance of the guidelines under 6103(i) could have and should have prevented this controversy from arising in the first place.

Since no further action has taken place at the district court level, we in the tax department are unable to state what the disposition of the request for the subpena is. Yet that fact, plus the original decision not to proceed under section 6103, points out the weakness of that section as it relates to State tax administration.

Massachusetts now takes the position that 6103(i) must be amended to provide that the exclusive procedure for subpena of State tax returns is under 6103, and further, if State tax returns are sought, that the State tax official whose returns are being sought in the subpena shall become a party to the hearing before the judge.

The present section 6103 is ex parte and the State, with all of its revenues which it may claim is in jeopardy, has to rely on a presentation of its case by one who is not in possession of all of the revenue consequences, at least, and, at worst on one who is prejudiced with respect to the State's interests.

If that condition should now occur in Massachusetts, we feel sure that the court will not be convinced that the tax returns sought are probative of the issue. This, in fact, is the return, a whole series of these monthly returns which are being sought in the subpena [exhibit displayed].

These returns are called the meals tax return. That return contains only one line of substantive information and in all it only contains five lines. The second to the fifth lines are merely arithmetic computations, one of which is printed on the return itself and is sent out by the tax department, and that is the 5-percent tax rate.

This taxpayer was a corporate taxpayer. All information that is on the meals tax return is also found on the Federal corporate tax return form 1120.

Now, the State tax commissioner has, of course, no knowledge of why the subpena was not sought under section 6103, nor why the Federal corporate income tax return was not subpenaed instead of the State meals tax return.

The subpena was requested not under 6103 but under the supremacy clause. As the appeal court said in deciding the case, "We see no reason why if the Federal prosecutions are not unduly hindered by the restraints of 6103 they would be so hindered by applying the same rules to State tax returns."

The court further stated, "We think the key has already been forged by the Congress in legislating in 6103 the conditions under which Federal tax information may be made available to Federal officials for nontax criminal purposes." By the suggestive amendments that we are requesting at this point, that very same principle would apply to the subpenaing of State tax returns.

Now, it is presumptuous on our part to say that the meals tax return is not probative of the issue or that it is not the only reasonable source for the information that is sought. But if it is, the State has an interest in making certain that all of its position becomes known to the court before confidentiality is breached.

I have made statements with respect to my position as a spokesman for all the States. With respect to the amendments which I am suggesting to you, I speak only for Massachusetts, but we will, through our organization, the National Association of Tax Administrators, solicit the support of all of the other States for these amendments to section 6103.

With all of the testimony that went on today, Mr. Chairman, nothing was said about the impact on State tax administration and State tax returns. Yet, the only case which is in the courts and which the courts have decided—on this issue—is a State tax case.

We think that the time has come to recognize what we thought was the original agreement back in 1976. It should be continued. We are making no attempts to change the substance of any of the three rules. We simply ask that if State tax returns are sought under a subpena that the exclusive method shall be that provided under section 6103(i) and the State tax administrator be a party to the proceeding.

[The following statement was subsequently received:]

STATEMENT OF THE MASSACHUSETTS DEPARTMENT OF REVENUE, BY OWEN L. CLARKE, DEPUTY COMMISSIONER MULTISTATE

My name is Owen L. Clarke, Deputy Commissioner Multistate, Massachusetts Department of Revenue. I am a past president of the National Association of Tax Administrators and was the president of the organization in 1976, when the IRC was last amended with respect to Section 6103(i). I participated, with other state tax administrators, in the discussions with the several federal agencies which were, at that time, involved with the various proposals and recommendations then under consideration.

As president of NATA, and tax commissioner in Massachusetts, I testified before the full Ways and Means Committee of the House and subsequently before the appropriate Senate Committees dealing with the whole question of confidentiality of tax returns and return information and with the important and sensitive relations between state tax departments and the Internal Revenue Service.

During that critical "Watergate Era" serious charges were raised, by some, that state tax department personnel were responsible for allowing unlawful and widespread disclosure of tax returns and information and that, as a result thereof, the then existing exchange of information agreements, which practically all states had with the Internal Revenue Service, ought to be cancelled and no further exchange of tax returns or information should be allowed.

The state tax administrators vigorously and, as subsequent amendments to Section 6103 IRC demonstrrate, successfully proved that not one single instance in the so-called "enemy list" and not one single state tax return, or federal tax return in the possession of any state tax department, was found among the many thousands of returns which were uncovered by federal authorities in places where they should not have been.

State tax authorities stated at that time, and they so state today, that the exchange agreements between the Internal Revenue Service and the states represent in all cases a most important part of state tax administration and in some instances are an absolute requirement.

As a result of those meetings and on the testimony of state officials before the Congress, not only were the exchange of information agreements retained, but they were, in fact, with the active participation of the states, strengthened and made more effective

The NATA and the state tax administrators have engaged in conferences and meetings with the IRS regularly since 1976, and on a frequent basis, to review and up-date those mutual assistance pacts.

Every state tax department has installed a system of guaranteeing that each of its employees is fully informed of all the provisions contained, not only in the agreements, but also in each state tax law, and of the penalties which are incurred by any employee who violates appropriate confidentiality provisions. In Massachusetts every employee, including each new employee, is required to sign an affidavit that they have read, and that they have an understanding of the confidentiality provisions of our law and of the mutual assistance agreements, and a copy of each of these is given to each employee to retain in his possession.

State tax administrators state unequivocally, and without reservation, that confidentially of tax returns and tax return information, filed with them by their taxpayers, is the very keystone of revenue payment. Without confidentiality, or with a lack of respect by taxpayers that the tax department seriously protects confidentiality, voluntary payment of taxes, which the entire system is built upon, will substantially diminish.

Every student or analyst of the American system of taxation comes to the same conclusion. Taxation experts from other countries repeat, over and over again, that the voluntary disclosure and payment of taxes by Americans is the most baffling phenomenon for them to understand. They also conclude that the principle of confidentiality which exists between taxpayer and tax department is the foundation for such reporting and payment. They carefully note, however, that the American people are deeply convinced that when they file a tax return with a tax department such return will not show up the next week as a gossip item at a cocktail party.

Both federal and state tax administrators must, at all costs, make certain that this respect which the American taxpayers have for confidentiality is not destroyed or weakened. The taxpayers may rant and rave over the amount of taxes they have to pay—the rapacious tax collector has his hand in my pocket—no matter how much I pay the government still wants more—if you open your mouth in the tax collector's office he will take the gold out of your teeth—but the one statement you never hear from a taxpayer is that his return can be or is revealed to every Tom, Dick and Harry that comes along.

When, therefore, in 1976 the conflicting issues of privacy of information, and the proper and necessary disclosure of information was presented to the Congress for resolution, we feel that, at least in the field of tax administration, a positive, viable and acceptable solution was reached in the present provisions of Section 6103 as they were enacted into law in that year.

When, however, the discussions turned to the problem of using tax returns, and/or related information, for evidence in matters not directly involving tax administration, or the violation of tax laws, strong representations were made, both by state and federal tax authorities, that under no circumstances should the returns of either tax agency ever be used except in instances exclusively related to tax cases.

Yet the very important concerns of experts in the field of Criminal Justice to protect the general public against both organized and individually perpetrated crimes—convinced most tax officials that major injury could reasonably be expected to occur if a total prohibition against the use of tax returns in non-tax criminal proceedings were to be enacted.

This latter position prevailed even though many state laws then, and now, provide for such prohibition.

The question then came—how far should the principle of confidentiality be breached and under what circumstances?

All of the testimony before this Subcommittee on Oversight here today, relating to use of tax returns in non-tax matters, has been concerned only with the use of federal tax returns. While this is a federal law and obviously, federal agencies play the major role in administering the law, this committee must recognize that Section 6103 IRC is directly and importantly tied to state and local tax administration.

Section 6103 IRC was amended in 1976 only full and substantive recommendations were made by state tax administrators and were agreed to by those involved in drafting the proposals. The states organized their support for the amendments by directly contacting their congressmen and senators on the interests which each state had at stake.

As president of NATA I directly participated in the drafting of the state related amendments to Section 6103 IRC. Most state tax administrators thought, as indeed I thought, that if any state tax returns were to be summoned in any non-tax matter that such returns would be sought under the accepted provisions of Section 6103(i).

It was, and in my opinion still is, the states' position that no state tax administrator should "willy-nilly" refuse to allow a state tax return to be used in a non-tax matter, when a serious crime has been committed, and the information on such state return is extremely important to and very substantive in proving such crime.

It is equally the state tax administrators' position that no public prosecutor should "willy-nilly" be allowed to use state tax returns in prosecutions on non-tax crimes simply because it would be of some aid and assistance to him to have such returns available.

The guidelines which were set forth for obtaining state tax returns—the three tests which have been discussed here in detail today—were thought by us to be the ones which would be used exclusively if state tax returns were to be used in a non-tax matter. They are reasonable and acceptable by the states if they are used.

However, state tax administrators generally and, of course, the Massachusetts tax commissioner in particular, now know that the agreed upon guidelines are not the exclusive way for seeking state tax returns.

In April of 1981, the United States Attorney for Massachusetts presented a case to the federal grand jury in Boston involving arson—a non-tax case. The grand jury issued a subpoena duces tecum to L. Joyce Hampers, Commissioner of Revenue, ordering her to appear and testify before the grand jury and bring documents relating to the sales tax on meals and beverages for the corporate owner of a restaurant for the period from October 1977 to October 1978. The commissioner moved to quash the subpoena and was denied and was ordered to appear.

After again refusing, the court held the commissioner in contempt and an appeal was taken to the Court of Appeals for the First Circuit. A record of this case including all the briefs submitted by Massachusetts, and many other states which joined in amici curiae, is in the file of your committee.

The Circuit Court, as you know, reversed the lower court and remanded the case to the lower court to instruct the federal authorities to procede under Section 6103(i) if they need those returns.

Obviously Massachusetts considers confidentiality of utmost importance even to the unhappy possibility of the imposition of a jail sentence to protect it. The federal experts who have testified here today have without exception emphasized the tremendous importance of confidentiality in the protection and, indeed, on the production of federal revenue. If that be so, and recognizing the enormous resources available to the Internal Revenue Service to ensure compliance with federal tax reporting and payment requirements, how much more important is confidentiality to state and local governments with their much more limited resources.

Since as of this date, no further action has taken place at the U.S. District Court level on the remand or, to our knowledge at the grand jury level we are unable to state what the dispostion of the request for subpoena is.

Yet that fact, plus the original decision not to proceed under Section 6103(i), now reveals a glaring weakness in that section as it relates to state tax administration.

Massachusetts urgently recommends that Section 6103(i) be amended to provide the following:

I. Section 6103(i) shall contain a separate subsection relating to state tax administration and to the use of state tax returns by federal officials in a non-tax criminal proceeding.

II. Section 6103(i) shall be the only and exclusive provision under which state tax returns, return information or third party information can be subpoened.

III. The state tax administrator whose returns and/or information is sought by the subpoena shall be a party to the hearing before the judge with equal standing with the federal official seeking the issuance of the subpoena.

IV. The present standards in Section 6103(i) shall not be amended with respect to Section 6102(i)(1) when state tax returns and/or information is sought.

V. Any state tax official who, pursuant to a court order issued under Section 6103(i)—as amended by these proposals—produces such returns and/or information, or who is compelled thereunder to testify before an appropriate federal agency, shall not be liable for any criminal or civil sanction even if the law of that state or any regulation issued by such state prohibits the disclosure of such return and/or information.

These amendments are required if the unfortunate case of "Re: L. Joyce Hampers" is not to be repeated. There is, of course, no assurance that the decision of the First Circuit will be followed by the other federal circuits. It also should be noted that the case was not appealed by the Justice Department to the U.S. Supreme Court.

The Massachusetts tax commissioner, of course, has no knowledge of why the subpoena was not sought under Section 6103(i) nor why the federal corporation tax return was not subpoened instead of the state's meals tax return. All we know is that in the Massachusetts district the subpoena was sought under the Supremacy Clause and that the federal corporation tax return contains all the information that is on the meals tax return and substantially more.

It is presumptuous on our part to say that the meals tax return is not probative of the issue before the grand jury, or that it is not the only reasonable source of the information sought but if it is, then the state has an interest in making certain that its position becomes known to the court before confidentiality is breached.

The present Section 6103(i) is ex parte and the state, with its claim that its revenues are in jeopardy if the subpoena issues, must, at best, rely on a presentation of its facts by one who is not in possession of all the revenue consequences and, at worst, is prejudiced with respect to the states or local governments interests.

We cannot state too strongly that, because of the vital state interests which this committee recognized in 1976, and responded to with the drafting assistance of state tax administrators, no amendments in Section 6103(i) be made without the participation of state tax administrators and with their concurrence.

The amendments which I have suggested here today will be circulated to all state tax departments by the National Association of Tax Administrators and I urge this committee to work with us in protecting state and local tax administration.

What the states seek by these amendments in no way interferes with federal agencies dealing with other federal agencies but is strictly limited to federal agencies dealing with state and local tax administrators.

Chairman **Rangel**. It makes a lot of sense, Mr. Clarke, and I thank you for your patience in bringing this matter to the attention of the committee. Indeed, the State of Massachusetts is fortunate to have someone that is that concerned with the right of privacy of its citizens.

It would be very important to the committee if you could persuade your colleagues in the national association to join with you in that statement. It will help us with members outside of the committee.

It makes a lot of sense because to the taxpayers it really does not make any difference whether they are being abused by the Federal Government or the State system. So, we have to make certain that we have one criteria.

I am glad that you cared enough and took time to bring that to the attention of the committee.

Thank you very much.

Mr. **Clarke**. Thank you.

[The following was subsequently received:]

National Association of Tax Administrators,
Washington, D.C., March 16, 1982.

Hon. Charles B. Rangel,
Chairman, Subcommittee on Oversight, Committee on Ways and Means, House of Representatives, Washington, D.C.

Dear Congressman Rangel: On behalf of the Executive Committee of the National Association of Tax Administrators, there is herewith submitted to the Subcommittee on Oversight a statement on the tax privacy issues which were the subject of the Subcommittee's hearing on December 14, 1981.

The National Association of Tax Administrators is an organization of the revenue departments of the fifty state governments. It submits this statement because of the state tax agencies' deep concern that bills currently before Congress would have the effect of depriving state tax returns of the protection they now have under state confidentiality laws.

In doing so, the Executive Committee joins in the statement on the privacy of state tax returns presented to the Subcommittee by Owen L. Clarke, on behalf of the Massachusetts Department of Revenue, and it respectfully requests that the Subcommittee consider the adoption of the enclosed amendment of Section 6103(i) should it recommend a change in that section of the Internal Revenue Code.

Your consideration of the states' concerns in this matter is very much appreciated.

Sincerely,

LEON ROTHENBERG,
Executive Secretary.

STATEMENT OF THE EXECUTIVE COMMITTEE OF THE NATIONAL ASSOCIATION OF TAX ADMINISTRATORS IN SUPPORT OF THE MASSACHUSETTS DEPARTMENT OF REVENUE STATEMENT TO THE SUBCOMMITTEE ON OVERSIGHT

The Executive Committee of the National Association of Tax Administrators joins in the statement submitted by the Massachusetts Department of Revenue to the Subcommittee on Oversight, House Committee on Ways and Means at the hearing held on December 14, 1981 on taxpayer privacy issues and proposals to amend Section 6103(i) of the Internal Revenue Code, the provisions of the Tax Reform Act of 1976 relating to the disclosure of tax return and return information for nontax purposes.

The NATA Executive Committee, in particular, joins in the following recommendations:

1. Section 6103(i) shall contain a separate subsection relating to state tax administration and to the use of state tax returns by federal officials in a nontax criminal proceeding.
2. Section 6103(i) shall be the only and exclusive provision under which state tax returns, return information or third party information can be subpoenaed.
3. The state tax administrator whose returns and/or information is sought by the subpoena shall be a party to the hearing before the judge with equal standing with the federal official seeking the issuance of the subpoena.
4. The present standards in Section 6103(i)(1) shall not be amended with respect to Section 6103(i) when state tax returns and/or information is sought.
5. Any state official who, pursuant to a court order issued under Section 6103(i)—as amended by these proposals—produces such returns and/or information, or who is compelled thereunder to testify before an appropriate federal agency, shall not be liable for any criminal or civil sanction even if the law of that state or any regulation issued by each state prohibits the disclosure of such return and/or information.

The National Association of Tax Administrators is an organization of the tax administrators of the state tax agencies of the 50 states. NATA participated in the discussions which led to the enactment of Section 6103(i) in 1976. It has since been in close communication with the Internal Revenue Service in regard to matters relating to confidentiality of federal and state returns and return information.

STATUTORY AMENDMENT

Following the December 14, 1981 hearing, the Massachusetts Department of Revenue drafted a statutory amendment which incorporated the previously listed recommendations. A copy of that amendment is enclosed.

If the Subcommittee on Oversight recommends legislation to amend Section 6103(i), the NATA Executive Committee requests the Subcommittee to include the enclosed amendment in its bill. It proposes the inclusion of this amendment because the confidentiality of state tax returns is a vital element in effective and equitable state tax administration and because changing the present provisions of Section 6103(i) without recognition of the states' special concerns would conflict with existing laws in many states and remove the protection such laws now give to state tax returns and return information.

STATE CONCERNS OVER THE CONFIDENTIALITY OF TAX RETURNS

The federal subpoena of state tax returns has been a continuing concern in state tax administration. In recent years, federal authorities have used federal subpoenas increasingly to obtain state tax returns and return information for nontax purposes. A NATA survey has shown that more than a third of the income tax states have received federal subpoenas for tax returns for nontax purposes.

In 1979, in response to the state's concern over these developments, the National Association of Tax Administrators, at its Forty-seventh Annual Meeting, adopted a resolution which called upon federal authorities to prohibit federal agencies and personnel from subpoenaing information which is confidential under state law. A copy of that resolution accompanies this statement.

Federal authorities continued to subpoena state tax returns into 1981. Last year, the U.S. Court of Appeals, First Circuit, *In Re L. Joyce Hampers* (651 F. 2d 19) denied federal access to a Massachusetts tax return because the requirements of Section 6103(i) had not been observed. The *Hampers* decision was a significant development in the states' efforts to protect the confidentiality of their tax returns. However, bills now before Congress would amend Section 6103(i) so as to eliminate the provisions on which the *Hampers* decision was based, namely that in a nontax criminal case, the tax return or return information sought constitutes probative evidence and it is evidence which could not reasonably be obtained elsewhere.

DISTINGUISHING STATE REQUIREMENTS FOR TAX RETURN CONFIDENTIALITY FROM FEDERAL REQUIREMENTS

The amendment proposed by the Massachusetts Department of Revenue, through a separate subsection in Section 6103(i), would distinguish requirements of confidentiality of State tax returns and return information from those for federal tax returns, when the information was sought in connection with nontax criminal proceedings. It would preserve the present Section 6103(i) standards for state tax returns in the event those standards were changed for federal purposes, and it would make the state tax administrator equal in court to the federal official seeking the issuance of the subpoena.

Since all of the states have laws protecting the confidentiality of tax returns, and in many, the disclosure of such returns for nontax purposes, even in response to a court order, may be in violation of state law, the NATA Executive Committee joins the Massachusetts Department of Revenue in recommending that any change in Section 6103(i) include a special provision to protect state tax administrators in such instances.

To permit the state tax administrator to represent his state adequately when a federal subpoena is sought, the NATA Executive Committee also joins in recommending that the state tax administrator be a party to the judicial hearing with standing equal to the federal officials seeking the issuance of the subpoena.

Also, in order to prevent the indiscriminate subpoenaing of state tax returns and return information, when the same information is available from federal and other sources, the NATA Executive Committee, with respect to state tax returns and return information, urges retention of the requirements in Section 6103(i) that the information sought be probative evidence and not reasonably obtainable elsewhere.

RESOLUTION ADOPTED AT THE FORTY-SEVENTH ANNUAL MEETING OF THE NATIONAL ASSOCIATION OF TAX ADMINISTRATORS, HELD IN MADISON, WIS., JUNE 10-13, 1979

RESOLUTION TWELVE

Whereas, federal agencies not engaged in tax administration have increasingly subpoenaed confidential state tax returns and state tax return information, and

Whereas, the release of such information for non-tax purposes is a violation of state law in many states and interferes with the states' commitment to their taxpayers that tax returns will be kept confidential and will be used for tax purposes only, and

Whereas, the subpoena of such records is inconsistent with the provisions of Section 6103 of the Internal Revenue Code relating to the confidentiality of federal tax return information transmitted to the states, now therefore, be it

Resolved, That the National Association of Tax Administrators notify the appropriate federal agencies of the Association's objection to such practices, and memoralize appropriate federal authorities to prohibit federal agencies and personnel from subpoenaing data which is confidential under state statutes.

STATE TAX ADMINISTRATORS DRAFT OF AMENDMENTS TO SECTION 6103(i) IRC

PROPOSED BY THE MASSACHUSETTS DEPARTMENT OF REVENUE

Section 6103(i) shall be amended by adding after Sec. 6103(i) (6) the following new section.

(7) STATE AND LOCAL TAX ADMINISTRATION.—

(a) Information from taxpayer.—A state or local return or taxpayer return information shall, pursuant to and upon the grant of, an order by a Federal district court judge as provided by this paragraph, issued only after notifying the appropriate state or local tax administrator and allowing such administrator equal status with the head of any Federal agency described in paragraphs (1)(A) and (1)(B), be open, but only to the extent necessary as provided in such order, to officers and employees of a Federal agency personally and directly engaged in and solely for their use in preparation for any administrative or judicial proceeding (or investigation which may result in such a proceeding) pertaining to the enforcement of a specifically designated Federal criminal statute (not involving the tax administration) to which the United States or such agency is or may be a party.

Notwithstanding any other provision of Federal or state law to the contrary the provisions of this section shall be the sole and exclusive means by which state and local returns or taxpayer return information may be open to such officers and employees of any Federal agency described in this subparagraph.

(b) Application for order.—The head of any Federal agency described in subparagraph (A) or, in the case of the Department of Justice, the Attorney General, the Deputy Attorney General, or an Assistant Attorney General, may authorize an application to a Federal district court judge for the order referred to in subparagraph (A), provided that the appropriate state or local tax administrator is notified of the filing thereof. Upon such application and the allowance of such administrator to be heard on the same basis as the applicant, such judge may grant such order with respect to state and local returns or taxpayer return information if he determines on the basis of the facts submitted by the applicant and the appropriate state or local tax administrator that—

(i) there is reasonable cause to believe, based upon information believed to be reliable, that a specific criminal act has been committed;

(ii) There is reason to believe that such return or return information is probative evidence of a matter in issue related to the commission of such criminal act; and

(iii) the information sought to be disclosed cannot reasonably be obtained from any other source, unless it is determined that, notwithstanding the reasonable availability of the information from another source, the return or return information sought constitutes the most probative evidence of a matter in issue relating to the commission of such criminal act.

However, a state or local tax administrator shall not disclose any state or local return or return information under this paragraph if he determines and certifies to the court that such disclosure would identify a confidential informant or seriously impair a civil or criminal state or local tax investigation.

(c) Return information other than taxpayer return information.—Upon written request from the head of a Federal agency described in subparagraph (A), or in the case of the Department of Justice, the Attorney General, the Deputy Attorney General, or an Assistant Attorney General, a state or local tax administrator shall disclose state or local return information (other than taxpayer return information) to officers and employees of such agency personally and directly engaged in, and solely for their use in preparation for any administrative or judicial proceeding (or investigation which may result in such a proceeding) described in this subparagraph (A).

Such request shall set forth—

(a) the name and address of the taxpayer with respect to whom such information relates;

(b) the taxable period or periods to which the return information relates;

(c) the statutory authority under which the proceeding or investigation is being conducted; and

(d) the specific reason or reasons why such disclosure is or may be material to the proceeding or investigation.

However, such state or local tax administrator shall not disclose any state or local return or return information under this paragraph if he determines that such disclosure would identify a confidential informant or seriously impair a civil or criminal state or local tax investigation. For purposes of this paragraph, the name and address of the taxpayer shall not be treated as taxpayer return information.

(d) Disclosure of return information concerning possible criminal activities.—A state or local tax administrator shall not disclose or be required to disclose to any Federal agency described in subparagraph (A) any state or local return or return information or information which may constitute evidence of a violation of Federal criminal laws.

(e) Use in judicial or administrative proceedings.—Any state or local tax return or return information obtanied under this paragraph may be entered into evidence in any administrative or judicial proceeding pertaining to enforcement of a specifically designated Federal criminal statute (not involving tax administration) to which the United States or an agency described in subparagraph (A) is a party but, in the case of any state or local return or return information obtained under this paragraph, only if the court finds that such state or local return or return information is probative of a matter in issue relevant in establishing the commission of a crime or the guilt of a party. However, any state or local return or return information obtained under this paragraph shall not be admitted into evidence in such proceeding if the state or local tax administrator determines and notifies the Attorney General or his delegate or the head of such Federal agency that such admission would identify a confidential informant or seriously impair a state or local civil or criminal tax investigation. The admission into evidence of any state or local return or return information contrary to the provisions of this paragraph shall not, as such, constitute reversible error upon appeal of a judgment in such proceeding.

(f) Penalties for disclosure of State or local tax return or taxpayer return information.—Notwithstanding any other Federal, state or local law to the contrary, any state or local tax administrator required under the provisions of this paragraph to open any state or local return or taxpayer return of information or return of information of other than taxpayer information or who pursuant to an order of the court is required to give testimony before any appropriate Federal agency shall not be subject to any sanctions, suits for personal damages or any penalties either civil or criminal.

All actions pursuant to this paragraph of a state or local tax administrator and all communications either written or oral shall be determined to be taken or made in accordance with and in execution of the official duties of such administrator and shall not be determined by any court to be personal or private actions or communications.

Chairman RANGEL. We may forward some questions to you so that you can include it with your written statement.

We have the Department of Justice here, Mr. Edward Schmults, Deputy Attorney General.

I know that you have been in and out with us all day, and I thank you for your patience. If you do have a written statement, that full statement will be entered into the record at this time, and you can proceed as you find convenient.

STATEMENT OF EDWARD SCHMULTS, DEPUTY ATTORNEY GENERAL, DEPARTMENT OF JUSTICE

Mr. SCHMULTS. Thank you, Mr. Chairman.

I do have a written statement that I would like to submit for the record, which is 22 pages. What I would like to do, with your permission, is to summarize that for you, if I may.

Chairman RANGEL. Without objection.

Mr. SCHMULTS. Thank you.

I welcome the opportunity to discuss this morning the several unnecessary impediments the Department of Justice has encountered under the disclosure and summons enforcement provisions of the Tax Reform Act of 1976.

We have submitted for the record a comprehensive and annotated statement that enumerates and explains the various difficulties and suggests appropriate remedies that preserve taxpayer privacy and the self-assessment system of tax collections.

I intend to summarize that statement for the convenience of the committee and then respond to any questions.

In seeking tax disclosure and summons amendments, the Department confronts practical difficulties in demonstrating the adverse effects which existing law has upon law enforcement. The proof requires documentation of a negative, such as identifying particular crimes that went unprosecuted because of these statutory impediments.

The Department concedes that the number of criminal tax and nontax cases we are losing due to statutory obstacles is unknown. Criminal cases do not lend themselves to categorization on the basis of the sources of evidence used in proving the offense.

Indeed, most cases, particularly sophisticated cases, are developed based upon information obtained from a wide variety of sources. Further, we have no charter to divert our limited resources from law enforcement to investigating and quantifying the adverse effects of particular congressional enactments.

Despite these handicaps, we have assembled information which corroborates the view that the effects of tax disclosure and summons restrictions upon law enforcement are very serious indeed.

First, we know based upon disclosure statistics maintained by the IRS that law enforcement access to tax information has declined precipitously in the aftermath of the 1976 act, perhaps to less than 20 percent of fiscal year 1975 levels.

This dramatic decline is particularly significant because tax disclosures would have been expected to increase substantially after 1976 when Federal law enforcement agencies intensified their attack upon sophisticated criminal activity.

For example, Drug Enforcement Administration arrests of class I and II offenders, primarily high-level narcotics traffickers and their financiers, have increased by almost one-third during the 3-year period from fiscal year 1978 to fiscal year 1980. From fiscal year 1975 to fiscal year 1980, case filings for betrayal of office were up 35 percent, racketeering up 19 percent, and wire and mail fraud up 24 percent.

During the same period, Federal investigations and prosecutions of street crimes, such as motor vehicle theft, bank robbery, and theft from interstate shipments, declined. In sum, although the Department is currently prosecuting more sophisticated cases requiring access to tax information than in 1976, our access to tax information has been sharply curtailed.

Second, statistics maintained by the IRS are noteworthy. In fiscal year 1974, IRS initiated 620 strike force cases. Since the tax disclosure and summons restrictions were enacted in 1976, that number has dropped by more than one-half.

Third, a 1980 survey conducted by the Department's Tax Division indicated that about half of the Federal prosecutors surveyed do not seek disclosure of tax information because of the cumbersome procedures, delay, and paperwork involved.

Despite significant efforts by headquarters officials in recent months to encourage use of tax information in appropriate cases, our understanding is that a more recent survey by the General Accounting Office indicates that the findings of the 1980 study remain valid.

These figures and findings are of serious moment, especially in an era of rampant crime.

Chairman RANGEL. You say the General Accounting Office report is valid or invalid?

Mr. SCHMULTS. No; it is valid, and the General Accounting Office findings indicate that the 1980 study of our Tax Divison remained valid. In other words, the General Accounting Office essentially came up with the same conclusions, Mr. Chairman.

Today, narcotics flood in the country to the point that economies of entire regions of the country are severely distorted by illegal narcotics profits, organized crime flourishes despite augmented law enforcement efforts, and virtually every other species of criminal activity is growing.

The total number of major criminal offenses reported in 1980 for the first time exceeded 13 million, up 55 percent during the past decade.

Support for tax disclosure amendments has solidified in recent months. By way of a brief chronology, the Senate Permanent Subcommittee on Investigations conducted hearings on illegal narcotics profits in December of 1979 and recommended a series of amendments to tax disclosure and summons enforcement law in early 1980.

Later that year, GAO testified in support of reforms to the disclosure provisions of the Internal Revenue Code. In September of 1980, the previous administration endorsed a proposal which has been introduced as S. 732 and H.R. 5102, introduced by Representative Gibbons of the 97th Congress.

This year, 66 Senators supported S. 732 as a floor amendment to the Economic Recovery Tax Act of 1981. That provision of the tax bill was deleted in conference, but the conferees agreed that early hearings would be held on the issue.

In August, the Attorney General's Task Force on Violent Crime, chaired by Judge Griffin Bell and Gov. James Thompson, endorsed tax disclosure amendments as a means of strengthening law enforcement efforts to control narcotics trafficking and organized crime.

In November, the Committee on Federal Legislation of the New York City Bar Association published a report endorsing most of the provisions of S. 732. On November 9, the Senate Subcommittee on Oversight of the IRS held hearings at which there was broad support for the great majority of the provisions of S. 732.

Finally, on November 19 the Department of Justice on behalf of the administration submitted its tax disclosure and summons enforcement proposal which was recently introduced as S. 1891 by Senators Roth, Rudman, Nunn, and Chiles. The disclosure provisions of the administration bill are similar to S. 732 and H.R. 1502.

There are five basic facts which we urge the subcommittee to consider in its deliberations on tax disclosure and summons enforcement legislation.

First, the administration is only supporting proposals which will scrupulously safeguard taxpayer privacy and the Nation's cherished system of self-assessment of taxes.

Second, law enforcement agencies are essentially information gathering and processing entities which must have reasonable access to information in order to do their jobs.

Third, the need for access to documentary information, particularly financial information, such as tax records, has increased greatly in recent years due to the emphasis placed on investigation and prosecution of sophisticated crimes such as narcotics trafficking, organized crime, public corruption, and a wide variety of fraud schemes, including fraud against the Government.

Fourth, tax disclosure restraints are only one of a series of recently enacted statutory restraints upon law enforcement access to information; this growth of privacy laws makes it essential that needlessly complex, cumbersome, and counterproductive paperwork be eliminated.

Finally, the resources of the Federal criminal justice system are limited with the result that any unnecessary and nonproductive requirements imposed upon law enforcement access to information reduce the ability of law enforcement agencies and courts to administer Federal criminal laws.

The specific problems experienced in the disclosure area are numerous and diverse. As is set out in more detail in my prepared statement, several provisions of the 1976 law are needlessly ambiguous and others are unnecessarily complex. The centralization of law enforcement authority to request tax information and the two-step procedure involved in securing return and related nonreturn information needlessly obstruct law enforcement.

The requirement that disclosure orders be issued only by U.S. district judges impedes timely rulings on disclosure applications. In several respects, the existing disclosure standards are inappropriate and unrealistic, a view shared by virtually every Federal judge who has considered a disclosure application.

The number of instances in which the IRS can notify other Federal law enforcement agencies of nontax crimes uncovered during IRS tax investigations should be expanded.

We also believe that the 1976 law is defective in failing to authorize access to tax information in fugitive cases or in important foreign intelligence investigations affecting vital national security interests.

The 1976 law should be amended to authorize IRS-initiated disclosures in life threatening and other emergency circumstances. Limited disclosure pursuant to a court order at the behest of a Federal official should also be permitted to foreign, State, and local law enforcement agencies.

Finally, the civil and criminal provisions of the 1976 law deter legitimate disclosures of tax information by IRS officials and should be modified.

In sum, we believe, based upon 5 years of experience, that the Tax Reform Act of 1976, well motived though that law was, failed to strike an appropriate balance between the interests of taxpayer privacy and the proper administration of criminal justice.

I wish to underscore for the committee that the administration's reforms preserve fundamental taxpayer privacy safeguards established in 1976 and do not jeopardize self-assessment of taxes. Although not exhaustive, the following provisions are illustrative of the administration's fidelity to taxpayer privacy.

Our proposal retains the requirement that Federal law enforcement officials obtain a court order to secure access to any tax return, individual or otherwise. Similarly, a court order is required to obtain any information submitted to the IRS by an individual taxpayer, even during an IRS audit.

The court order procedure requires a U.S. attorney, strike force chief, or higher level Department officials to approve the application and persuade a neutral and detached judicial officer, prior to any disclosure, that there is reasonable cause to believe the tax information sought is relevant to the commission of a specific Federal criminal offense.

To secure information obtained by the IRS from third parties, a formal written request is required by a supervisory level Federal prosecutor. The request must specifically allege a suspected Federal criminal violation and the relevance of tax information to that offense. This request procedure creates a "paper trail" of access to information and makes supervisory level Federal prosecutors answerable for their actions in obtaining access to on return information.

Moreover, consistent with existing law, our proposal narrowly limits the circumstances in which the IRS may initiate a disclosure of tax information to other Federal law enforcement agencies. Generally speaking, the IRS can report a nontax crime only if the corroborating evidence is gleaned from nonreturn information.

Exceptions to the rule of nondisclosure by the IRS are also created for emergency situations and referrals of a taxpayer's file to the Tax Division for criminal tax prosecution.

It speaks volumes for the administration's concern for taxpayer privacy that GAO proposals would authorize more expansive IRS reporting of nontax crimes. The Department opposes this expansion because it may engender a perception that the IRS routinely examines tax returns to search for evidence of nontax crime. Such a perception could threaten full tax reporting and collections.

Finally, our bill retains criminal and civil sanctions for violations of the statutory tax disclosure procedures, thereby insuring scrupulous compliance. Intentional violations are Federal crimes, and taxpayers are invested with a civil remedy for less serious violations of privacy rights.

In sum, the administration's proposed reforms are faithful to the privacy objectives of the 1976 act.

In the summons area, the IRS and the Department of Justice have experienced problems that fall under two major headings. First, existing summons procedures are exploited by taxpayers seeking to obstruct legitimate IRS tax investigations. We believe the procedures approved by the Congress in the Right to Financial Privacy Act of 1978 would fully protect taxpayer privacy and are less likely to be misused by tax protesters and other persons interested only in delaying IRS investigations.

We suggest substitution of procedures similar to those of the Financial Privacy Act for the procedures of section 7609 of the Internal Revenue Code.

Second, there is a substantial volume of unnecessary litigation concerning the issuance of IRS administrative summons for a criminal investigative purpose. This obstacle to criminal tax investigations should be eliminated.

In addition, we believe that IRS should have access to grand jury information developed during the course of a criminal tax investigation where it can be shown to a court that the information is sought for use in tax investigations.

In our view, all of these problems require prompt action by the Congress. It is for this reason that the administration has submitted a comprehensive legislative reform proposal. We believe that our proposal would enhance law enforcement without undermining the fundamental privacy safeguards established in 1976 or imperilling tax collection.

In conclusion, the administration urges your support for reforms of the disclosure and summons provisions of the Internal Revenue Code, reforms which, while modest in scope, will reap large law enforcement dividends at the expense of organized crime. The reforms are a foremost component of the criminal justice initiatives before the Congress.

I can assure you that the Department of Justice is eager to work with you and your staff to insure that appropriate amendments of the type I have described can reach fruition.

I will now be pleased to respond to any questions.

[The prepared statement follows:]

STATEMENT OF EDWARD C. SCHMULTS, DEPUTY ATTORNEY GENERAL, DEPARTMENT OF JUSTICE

Mr. Chairman and Members of the Subcommittee, I appreciate the opportunity to testify today regarding proposals to amend the tax disclosure and Internal Revenue Service summons restrictions enacted in the Tax Reform Act of 1976. As you know, a comprehensive tax disclosure amendments bill was introduced in the Senate earlier this year as S. 732; an identical bill has been introduced in the House as H.R. 1502. A summons enforcement bill has been introduced as S. 1010 and H.R. 1501. In November, the Administration submitted its own comprehensive disclosure and summons proposal which has been introduced as S. 1891. In most respects, the Administration proposal parallels S. 732 and H.R. 1502 in seeking to fine-tune the restraints upon law enforcement access to tax information for use in nontax criminal cases. The Administration proposal, like S. 1010, would also facilitate access by the Internal Revenue Service to the information it needs in connection with tax investigations. It is the view of the Administration that both of these access-to-information issues should be treated together.

THE EMERGING CONSENSUS FOR REFORM OF TAX DISCLOSURE LAW

The effect of tax disclosure restrictions upon law enforcement has been the subject of debate for more than five years. As late as 1979, there were more questions than answers on this issue. In March of 1979, the General Accounting Office concluded that the effects of the disclosure and summons provisions of the 1976 Tax Reform Act were largely unknown.[1]

But in late 1979 and 1980, evidence of the adverse effects of tax disclosure provisions upon law enforcement began to emerge, primarily as the result of hearings by the Senate Permanent Subcommittee on Investigations.[2] Those hearings and the information developed therein led to introduction in the 96th Congress of S. 2402, 2403, 2404 and 2405 and H.R. 6826, 6827 and 6828. The introduction of these bills resulted in further hearings in 1980 before the Senate Finance Subcommittee on Oversight of the Internal Revenue Service[3] and this Subcommittee.[4] During those Finance and Ways and Means Subcommittee hearings, the General Accounting Office testified in support of the need for amendments to the 1976 law. In 1980 the previous Administration endorsed a compromise proposal which was later introduced as S. 732 and H.R. 1502 of the 97th Congress.[5]

---

[1] "Disclosure and Summons Provisions of 1976 Tax Reform Act—Privacy Gains With Unknown Law Enforcement Effects," General Accounting Office, GGD-78-110, Mar. 12, 1979.

[2] Hearings on Illegal Narcotics Profits Before the Permanent Subcomm. on Investigations, Sen. Comm. on Govt'l Affairs, 96th Cong., 1st sess., Dec. 7 and 11-14, 1979; see also, Sen. Rep. 96-887.

This year, support for reforms has continued to build. In July, 66 Senators supported addition of S. 732 as a Floor amendment to the Economic Recovery Tax Act of 1981.[6] This action was supported by the National Association of Attorneys General.[7] Although the amendment was deleted in Conference Committee, the Conferees made a commitment to hold House and Senate hearings on the issue of tax disclosure amendments.[8]

On August 17, the Attorney General's Task Force on Violent Crime endorsed tax disclosure amendments as a means of strengthening the federal fight against violent crime, particularly narcotics trafficking.[9] Also in November, the Committee on Federal Legislation of the New York City Bar Association published an appraisal of the tax disclosure issue and recommended enactment of most of the provisions of S. 732.[10] On November 19, the present Administration formally submitted to the Congress its own tax disclosure and summons enforcement amendments proposal which had been unveiled during a November 9 hearing before the Senate Finance Subcommittee on Oversight. That hearing revealed that a number of the provisions of the Administration proposal are non-controversial.[11]

GENERAL FACTORS SUPPORTING TAX DISCLOSURE AMENDMENTS

At the request of the Subcommittee, my testimony today will focus primarily on the problems encountered during our five years of experience under the Tax Reform Act of 1976 rather than discussing the detailed provisions of the Administration or Congressionally initiated bills. Before describing our specific difficulties, I will seek to set out in summary fashion several general considerations which I believe should be borne in mind when addressing this issue.

1. *Law enforcement agencies are information gathering and processing entities.* First, the task of law enforcement agencies in our adversary criminal justice system is to gather and assemble the information necessary to establish all the elements of a criminal offense beyond a reasonable doubt. The information thus gathered and assembled is ultimately presented to courts so that justice can be administered. It is essential, therefore, that law enforcement officials have reasonable access to information if they are to fulfill their vital role in our criminal justice system.

2. *Need for access to tax information has grown.* Second, federal law enforcement agencies now rely much more heavily upon documentary information, and particularly documents of a financial nature, than ever before because of the recent emphasis upon the investigation and prosecution of sophisticated criminal offenses such as narcotics trafficking, organized crime, public corruption, and other white-collar crime. Unlike "street crimes", which can often be proved purely on the basis of eyewitness testimony, the investigation of sophisticated offenses requires painstaking analysis of documents to trace the complex maze of financial and other transactions which are involved—and which are frequently made intentionally complex in order to conceal illegal acts and illicit profits.

3. *Tax disclosure restrictions are only one of a series of statutory restraints upon law enforcement access to documents.* Third, it is seldom recognized that tax disclosure restrictions are not the only restraints upon law enforcement access to documentary information. Rather, there are other Federal laws such as the Fair Credit

---

[3] Hearings on S. 2402-S. 2405 Before the Subcomm. on Oversight of the IRS, Sen. Comm. on Finance, 96th Cong., 2d sess., June 20, 1981.

[4] Hearings on H.R. 6826, H.R. 6827 and H.R. 6828 Before the Subcomm. on Oversight, H. Comm. on Ways and Means, 96th Cong., 2d sess., July 30, 1980.

[5] Letter from President Carter to Senator Nunn, Sept. 9, 1980.

[6] Congressional Record of July 27, 1981, at S8513–S8532.

[7] Letter from C. Raymond Marvin, General Counsel, National Association of Attorneys General to all Members, House Ways and Means Committee dated July 28, 1981.

[8] H. Rep. 97–215 at 264.

[9] Final Report, Attorney General's Task Force on Violent Crime, 37–38.

[10] "Tax Returns as a Law Enforcement Resources," 36 the Record 492, Nov. 1981.

[11] Hearings on S. 732 Before the Sucomm. on Oversight of the IRS, of the Sen. Comm. on Finance, 97th Cong., 1st sess., Nov. 9, 1981 (unpublished); Department of Justice statement sets out major differences between S. 732 and Administration proposal.

Reporting Act of 1970 [12], the Privacy Act of 1974 [13], the Right to Financial Privacy Act of 1978 [14] and the Privacy Protection Act of 1980 [15] which limit law enforcement access to records. Taken together, these and other restraints upon law enforcement access to information, each of which has its own set of access procedures, create a labyrinth which law enforcement officials must negotiate in order to prosecute sophisticated criminal cases. It is important, therefore, that every effort be made to avoid needlessly complex, cumbersome and dilatory procedures in each of these various privacy laws if we are to deal effectively with the serious and sophisticated criminal offenses now receiving the priority attention of federal law enforcement officials.

4. *Investigative, Prosecutive And Judicial Resources Are Limited.* Fourth, restraints upon law enforcement should recognize that the resources of the criminal justice system are limited and that needless restraints translate into reduced enforcement of federal criminal laws. It should be borne in mind, for example, that the average federal prosecutor has a case load in excess of 120 cases per year [16] and that there are fewer federal district judges than there are Members of the House and Senate.[17] Yet the crime rate continues to increase. While we do not contend that privacy laws should be written for the convenience of law enforcement officials, we do believe that practical realities must be recognized and that scarce investigative, prosecutive and judicial resources made elimination of unnecessary and nonproductive restraints a matter of the greatest urgency.

5. *The goal must be a realistic balancing of competing interests.* We in the law enforcement community recognize the importance of protecting individual privacy interests and of avoiding any adverse impact upon our voluntary self-assessment tax collection system. At the same time, however, we are keenly aware of the public interest in the proper administration of justice. Moreover, we believe, based upon five years of experience, that the Tax Reform Act of 1976, well motivated though that law was, failed to strike an appropriate balance between the interests of taxpayer privacy and the proper administration of justice primarily because its procedures and requirements do not reflect a full appreciation of the realities of criminal investigation and prosecution. The amendments we propose, therefore, are intended to refine the 1976 law. The fundamental privacy safeguards established in 1976 by the Congress, such as the requirement of a court order to obtain returns, are retained. Although we believe that the cumulative effect of our proposals will substantially strengthen law enforcement, they are not a radical departure from the disclosure system established in 1976. Rather, what we seek is an informed balancing of the competing interests which takes proper account of the day-to-day workings of the criminal justice system.

SPECIFIC PROBLEMS—THE DISCLOSURE AREA

The problems experienced under the 1976 law are numerous and diverse. The following are the more significant difficulties which we seek to remedy.

1. *Complexity and ambiguity.* Under existing law, a prosecutor seeking access to tax information is confronted with four different definitions: "return" [18], "return information" [19], "taxpayer return information" [20], and "return information other than taxpayer return information" [21]. We believe that this system of definitions is needlessly complex and that the purposes of the 1976 act can be served by using two definitions: "return information" and "nonreturn information." In addition to being

---

[12] Credit reports are available for law enforcement purposes only pursuant to court order, 15 U.S.C. 1681(b)(1).

[13] Generally, information in federal "systems of records" is available only pursuant to formal law enforcement request or court order, 5 U.S.C. 552a(b).

[14] Information held by "financial institutions" is subject to an elaborate series of overlapping restraints which vary depending upon the form of process utilized, 12 U.S.C. 3401-3422.

[15] Search warrants directed at third parties are subject to certain statutory and regulatory limits, 42 U.S.C. 2000aa-11 et seq.

[16] "Statistical Report", United States Attorney's Office, fiscal year 1980 at 7 (122.3 cases per Assistant United States Attorney, combined criminal and civil caseload).

[17] The Administrative Office of U.S. Courts advises that there were 471 active U.S. District Judges as of Nov. 30, 1981.

[18] 26 U.S.C. 6103(b)(1).

[19] 26 U.S.C. 6103(b)(2).

[20] 26 U.S.C. 6103(b)(3).

[21] 26 U.S.C. 6103(i) (2) and (3).

less cumbersome, these definitions more accurately describe the information covered [22] and also conform to the two-part disclosure procedure enacted in 1976 [23].

The 1976 Act is ambiguous as to the uses to which tax information can be put once obtained by federal prosecutors. This ambiguity has been largely resolved by IRS regulations, but few federal prosecutors work regularly with those regulations. We believe, therefore, that the tax disclosure statute should make clear, consistent with current IRS regulations, that a prosecutor may properly disclose tax information to investigative agents and other support personnel assisting him in an investigation or prosecution and that information can be disclosed to a federal grand jury. Such clarifications are consistent with existing practice and do not, therefore, adversely affect taxpayer privacy interests or tax administration. They do, however, avoid needless detours by busy prosecutors through copious IRS regulations simply to secure information for use in a nontax criminal investigation or prosecution.

2. *Centralization of request authority and two-step disclosure process.* Under existing law [24] prosecutors must seek approval from high-level Justice Department officials in Washington before going to court to seek a tax disclosure order or before requesting nonreturn information. This results in additional paperwork and delays the process of securing disclosure. High-level federal prosecutors in the field (United States Attorneys and Organized Strike Force Chiefs) should be authorized to apply to a court for a disclosure order and supervisory-level federal prosecutors in the field (if designated by the Attorney General) should be authorized to request nonreturn information.

Second, under existing law a court order only authorizes disclosure of return information; a separate request must be filed to secure related nonreturn information. This produces needless paperwork. If a federal prosecutor can make the showing required to persuade a neutral and detached judicial officer to order disclosure of the most stringently protected information held by IRS (i.e., returns and other information obtained from the taxpayer), that order should also authorize disclosure of any related information held by IRS which is subject to less stringent safeguards (i.e., information obtained from third parties).

Third, the special admissibility rules [25] should be deleted and admission of tax information into evidence made consistent with the Federal Rules of Evidence which govern all other forms of evidence.

3. *District judge requirements.* Existing law [26] requires that applications for disclosure orders be considered only by busy United States District Judges. To reduce the burden on District Judges and to increase the availability of judicial officers empowered to consider disclosure applications, United States Magistrates as well as District Judges should be authorized to consider disclosure applications. As we have frequently noted, U.S. Magistrates are currently authorized to perform other important judicial functions such as issuance of search warrants.[27] Because a Magistrate is competent to issue a warrant authorizing the search of a citizen's home, he should also be competent to determine whether information held by the IRS can be disclosed to a United States Attorney or Strike Force Chief.

4. *Inappropriate disclosure standards.* Under existing law, prosecutors face a "Catch-22" situation in seeking disclosure of tax information. For example, the literal terms of the statute require a showing of "probity" of the information [28] before disclosure can be ordered. The "probity" requirement was apparently taken from evidentiary law where it is normally applicable in situations in which all parties to the litigation have access to the information and the question is whether that information should be admitted at trial as probative of a matter in issue. In the tax disclosure context, however, a prosecutor does not have access to the information he is seeking and cannot reasonably be expected to demonstrate its probity. In fact, situations have occurred in which disclosure orders were issued only to learn that the taxpayer in question had not filed returns for the years in question. A prosecutor

---

[22] E.g., "return information other than taxpayer return information" is in reality information obtained by the Service from sources other than the taxpayer or his representative. The term "nonreturn information" more accurately describes this category of information.

[23] Both existing law and the Administration proposal are characterized by a two-track disclosure system: disclosure of "return information" requires entry of a court order while "nonreturn information" does not. The definition structure should conform to this disclosure structure for purposes of clarity.

[24] 26 U.S.C. 6103(i) (1)(B) and (2).

[25] 26 U.S.C. 6103(i)(4).

[26] 26 U.S.C. 6103(i)(B).

[27] Rule 41, Fed. R. Cr. P.

[28] 26 U.S.C. 6103(i)1)(B) (ii) and (iii).

cannot know, therefore, whether the evidence he seeks even exists, much less that it is "probative". The appropriate test in this context is "relevance."

Most courts have interpreted present law in the light of reason and experience to require a showing only of those facts a prosecutor can reasonably be expected to demonstrate: (1) that there is reasonable cause to believe a specific criminal act has occurred, is occurring or will occur; (2) that there is reasonable cause to believe the tax information sought is or may be relevant to that offense; and (3) that the information will be used solely for the purposes of investigating and prosecuting that offense. We believe these standards, which are the ones virtually every court considering an application for disclosure of tax information has applied, should be substituted for the inappropriate and unrealistic standards of existing law. The existence of the current standards in statutory law can lead to inconsistent judicial results[29] and are so rigorous on their face as to discourage prosecutors from applying for a disclosure order[30].

5. *Prosecutors unaware of crimes known to IRS.* IRS agents sometimes come across evidence of serious nontax crimes during the course of their tax investigations. In many cases, other federal law enforcement agencies are totally unaware of these offenses. In such circumstances, of course, the court order and formal written request disclosure provisions of current law are of no utility because federal prosecutors do not have any basis for initiating a court order or request. Although existing law permits IRS to initiate reports of nontax crime[31], the circumstances in which this can be done are too limited.[32] We believe that the number of instances in which IRS initiates reports of nontax crime should be expanded in ways which do not undermine taxpayer privacy or our voluntary self-assessment income tax system. More specifically, we suggest three changes in existing law to encourage IRS to report nontax crimes to the appropriate federal law enforcement agency. First, we suggest that reporting of nontax crimes should be mandatory rather than discretionary. Second, we recommend that reports of crime should be permitted to the extent that a crime is reflected in books and records of a legal entity where the IRS has reasonable cause to believe the legal entity is a sham set up to facilitate crime or is being operated for narcotics, organized crime or other illicit purposes. Third, we suggest that when a tax case is referred to the Tax Division of the Department of Justice for criminal tax prosecution, any informaition in the file evidencing nontax crime should be disclosed to the Criminal Division for nontax criminal investigation and prosecution.

6. *No fugitive access.* Return information may not now be disclosed for use in connection with efforts to locate fugitives from justice.[33] Yet the information furnished on tax returns often produces valuable leads that can assist in determining the whereabouts of a fugitive. We suggest therefore, that the court order procedure be modified to permit disclosure of tax information for use in an investigation directed toward determining the whereabouts of a fugitive from justice for whom a judicial arrest warrant has been issued.

7. *No foreign intelligence access.* Return information is not now available to federal intelligence agencies in connection with investigations directed at espionage and other activities being carried out by foreign powers and terrorist groups. Moreover, we believe that this result was unintended by the Congress and reflects a belief that foreign intelligence and counterintelligence access could be obtained pursuant to the general court order procedures of 6103(i)(1). In practice, however, court facilities and personnel do not possess the security features and clearances necessary for consideration of sensitive intelligence matters.[34] Further, because section 6103(i)(1) limits disclosure of tax information to that which evidences elements of a criminal offense, those investigations conducted solely for the purpose of collecting intelligence are precluded access to return information. Therefore, we propose a new procedure, patterned upon but more restrictive than the foreign intelligence access provision of the Right To Financial Privacy Act[35], by which tax information may be obtained

---

[29] E.g. *United States* v. *Praetorius*, 451 F.Supp. 371 (E.D.N.Y. 1978)).

[30] *See*, Tax Division Survey Regarding 26 U.S.C. 6103, Mar. 28, 1980.

[31] 26 U.S.C. 6103(i)(3).

[32] IRS-initiated disclosures are permitted only if based upon third-party information.

[33] 26 U.S.C. 6103(i)(1) limits disclosures of tax information to that information evidencing elements of the criminal offense and does not, therefore, permit disclosures for purposes of determining the whereabouts of a fugitive.

[34] Court clerks, court reporters, secretaries and law clerks do not normally have security clearances required to handle classified information; courts also generally lack the special safes and other facilities necessary to store classified information.

[35] 12 U.S.C. 3414(a).

by the Federal Bureau of Investigation and the Central Intelligence Agency for use in legitimate foreign intelligence and counterintelligence investigations.[36]

8. *No provision for emergency disclosure.* There is currently no procedure by which IRS officials may disclose information necessary to prevent an imminent threat to human life or safety, serious property damage, or flight from prosecution. Although we anticipate that it will be rare that IRS officials would have occasion to use such authority, the fact remains that the approximately 88,000 IRS employees review hundreds of thousands of tax returns each year (together with a myriad of other documents) and conduct interviews of thousands of persons. During this process, IRS officials may encounter information requiring a report to other federal law enforcement agencies on an emergency basis. But even though IRS officials maintain that they would report, for example, information evidencing a possible threat to the life of the President, such a report, if based on return information, would expose the reporting official to potential civil and criminal prosecution. There should be a carefully worded emergency exception to the general disclosure rules similar to that provided in the Right To Financial Privacy Act.[37]

9. *No provision for disclosure to State officials.* Federal tax information may be provided on a massive scale to State tax authorities for State tax purposes [38], but no disclosure whatsoever is permitted to State law enforcement authorities for nontax criminal investigation or prosecution. Even to the extent that federal prosecutors obtain tax information for use in a bona fide federal criminal investigation and recognize upon reviewing the information that it evidences the commission of a State felony, the federal prosecutor is barred from providing the pertinent information to a State Attorney General or District Attorney. We believe that it is inappropriate to require federal prosecutors to conceal evidence of serious State crimes and suggest that a procedure be established by which a federal prosecutor in possession of tax information evidencing a State felony can go to court to seek authority to redisclose that information to the appropriate State prosecutor.

10. *No provision for disclosure to foreign law enforcement officials.* Federal prosecutors are only able to secure information from foreign law enforcement officials if the United States can offer reciprocal discovery opportunities to foreign officials pursuant to a treaty or convention. The Congress recognized this in the tax area and authorized disclosures of tax information to foreign governments pursuant to international tax conventions [39]. But there is no similar provision authorizing disclosures pursuant to treaties of mutual assistance in criminal matters. As a result, we are unable to negotiate appropriate treaties affording federal officials access to foreign tax information. This shortcoming has an adverse effect on enforcement of narcotics trafficking and other criminal laws which involve international criminal conspiracies and transactions. We believe the law should provide for disclosure pursuant to mutual assistance treaties relating to criminal as well as tax matters.

11. *Civil and criminal provisions impede effective coordination.* Under existing law, any IRS official responsbile for erroneous disclosure of tax information is personally liable for civil damages.[40] Moreover, the same IRS official is potentially subject to criminal prosecution.[41] These severe penalties for unauthorized disclosure of tax information have an understandably chilling effect on IRS officials. We believe, consistent with the Privacy Act of 1974, the Right To Financial Privacy Act of 1978 and the Privacy Protection Act of 1980, that federal agencies rather than individual federal employees should be civilly liable for any unauthorized disclosure.[42] Moreover, the criminal provision governing unauthorized disclosure should make clear on its face that it is not applicable to disclosures made in a good faith belief that they were authorized by law. Finally, we feel that IRS cooperation in joint tax-nontax criminal invetigations should be expressly authorized.

SPECIFIC PROBLEMS: IRS ACCESS TO INFORMATION

In addition to problems encountered by federal law enforcement authorities in securing access to information held by the IRS, the Service itself faces severe difficulties, in part attributable to the Tax Reform Act of 1976, in obtaining information necessary to pursue its civil and criminal tax investigations. These problems occur in three major areas as follows:

---

[36] As the CIA is not involved in domestic investigations, the FBI would be the major beneficiary of the intelligence access provision although some overseas investigations by the CIA may require access to U.S. tax information, e.g., relating to a multinational corporation.

[37] 12 U.S.C. 3414(b).

[38] 26 U.S.C. 6103(d).

[39] 26 U.S.C. 6103(k)(4).

[40] 26 U.S.C. 7217.

[41] 26 U.S.C. 7213.

[42] All of these cited statutes make Federal agencies rather than individual Federal employees civilly liable for unauthorized disclosures of or access to protected information.

1. *Taxpayer abuse of statutory procedures to obstruct legitimate IRS investigations.* As revised in 1976, section 7609 of the Internal Revenue Code requires IRS to notify a taxpayer upon issuing an administrative summons for bank or other records at which point the taxpayer may block compliance with the summons merely by writing a letter to the bank or other record custodian. The buden then falls upon the IRS and the Department of Justice to petition a federal court for an order enforcing the summons. Once the petition for an enforcement order and supporting materials are prepared and filed by the Government and then reviewed by the court, a date is set at which the taxpayer may intervene and show cause why the IRS summons should not be enforced. Yet when that date arrives, the taxpayer frequently does not appear. Although an enforcement order is issued at that point, the IRS investigation has by then been delayed—for months—and the IRS, Justice Department and the court have expended considerable time and effort for no purpose. This and other provisions of section 7609 should be revised to conform generally to the Right To Financial Privacy Act of 1978.[43]

2. *Narrow reach of IRS administrative summonses.* Courts have interpreted the IRS administrative summons as being limited to investigative activities conducted prior to an "institutional commitment" to seek imposition of criminal sanctions.[44] This interpretation breeds unnecessary litigation and should be corrected through legislation.

3. *Obstacles to IRS access to grand jury information.* IRS agents, working as agents of the grand jury, often devote thousands of staff hours to grand jury investigations directed at tax crimes. We have encountered increasing difficulty in obtaining judicial authorization for the release of such grand jury information to IRS and support the enactment of legislation to resolve this problem.

CUMULATIVE EFFECTS OF UNNECESSARY AND UNDULY CUMBERSOME DISCLOSURE AND SUMMONS RESTRICTIONS

In seeking tax disclosure and summons amendments, we are sometimes asked to demonstrate the adverse effects which existing law has upon law enforcement. In effect, this amounts to a request that we document a negative. Sometimes we are even asked specifically how many cases we are unable to make because of these statutory impediments, in effect a request that we quantify a negative. The simple fact is that we do not know how many criminal tax and nontax cases we are not making due to statutory obstacles—because we are not making them. Moreover, criminal cases do not lend themselves to categorization on the basis of the sources of evidence used in proving the offense. Indeed, most cases, particularly sophisticated cases, are developed based upon information obtained from a wide variety of sources. Further, we believe that the Congress expects us to enforce the laws to the best of our ability in accordance with applicable restraints rather than to devote our limited resources to proving the adverse effects of particular Congressional enactments upon law enforcement operations.

Despite these factors, however, we do have information which indicates that the effects of tax disclosure and summons restrictions upon law enforcement are very serious indeed. First, we know based upon disclosure statistics maintained by the IRS that law enforcement access to tax information has declined precipitiously since enactment of the 1976 law, perhaps to less than 20 percent of fiscal year 1975 levels.[45] This dramatic decline is particularly significant in view of the fact that, but for the 1976 law, tax disclosures would have have been expected to increase substantially because of the increasing focus of federal law enforcement agencies upon sophisticated criminal activity. For example, Drug Enforcement Administration arrests of Class I and II offenders (primarily high-level narcotics traffickers and their financiers) increased by almost one-third during the three-year period from fiscal year 1978 to fiscal year 1980.[46] From fiscal year 1975 to fiscal year 1980, case filings for betrayal of office were up 35 percent[47], racketeering, up 19 percent[48], and wire and mail fraud, up 24 percent.[49] During the same period, federal investigations and prosecutions of "street crimes" such as motor vehicle theft, bank robbery and theft from interstate shipments declined. We are, therefore, engaged in many more sophisticated cases today then in 1976 requiring access to tax information. Yet our access to tax information is down sharply.

---

[43] See 12 U.S.C. 3410.

[44] *United States* v. *LaSalle National Bank*, 437 U.S. 298 (1978).

[45] Statistics cited at previous hearings use members of 1,800 for requests by the Department of Justice in 1975 as compared to 250 in fiscal year and 355 in fiscal year 1981. These numbers, however, are not comparable due to changes in recordkeeping required by the Tax Reform Act of 1976.

[46] 1,447 in fiscal year 1978 to 1,925 in fiscal year 1980.

[47] 123 in fiscal year 1975 to 181 in fiscal year 1980.

[48] 243 in fiscal year 1975 to 290 in fiscal year 1980.

Second, statistics maintained by the IRS are noteworthy. In fiscal year 1974, IRS initiated 620 strike force cases. Since the tax disclosure and summons restrictions were enacted in 1976, that number has dropped by more than one half.[50]

Third, a 1980 survey conducted by the Tax Division indicated that about half of the federal prosecutors surveyed do not seek disclosure of tax information because of the cumbersome procedures, delay and paperwork involved. Despite significant efforts by headquarters officials in recent months to encourage use of tax information in appropriate cases, our understanding is that a more recent survey by GAO indicates that the findings of the 1980 study are largely accurate today.

I would like to be able to say today that this is of no consequence—that the decline in access to tax information is due to a decline in the crime rate and that crime levels are at such low rates that failure to make cases against large scale narcotics traffickers, organized crime figures and other major criminal offenders is of little significance. As the Members of this Subcommittee know, however, the very opposite is the case. Narcotics are flooding the country to the point that economies of entire regions of the country are severely distorted by illegal narcotics profits, organized crime is growing despite expanded efforts to control it, and virtually every other species of criminal activity is growing to the extent that the total number of major criminal offenses reported in 1980 for the first time exceeded 13 million, up 55 percent since 1971. It is for this reason that the Department of Justice believes that unnecessary and nonproductive impediments to effective law enforcement cannot be accepted.

After five years of experience under the tax disclosure and summons provisions of the Tax Reform Act of 1976, we have identified fourteen areas, discussed above, where we believe legislative changes are urgently needed and clearly justified. While we recognize, from a pure legislative strategy perspective, that our prospects for Congressional action would be more favorable if our proposals were fewer and less technical, we do not believe that addressing any three or four of these problems alone would resolve the issue. Instead, it is the cumulative impact of all of these difficulties taken together that are impeding law enforcement efforts and it is for this reason that we have submitted a comprehensive package of amendments.

The proposal submitted by the Administration is the product of more than two years of study and drafting. We genuinely and sincerely seek relief from what we feel are unnecessary—and for the most part, unintended—impediments to effective law enforcement created by the Tax Reform Act of 1976. On behalf of the Administration and the law enforcement community, we are grateful for this opportunity to discuss our proposals and the need therefor and hope that you will see fit to accord our proposals your attention and support.

Chairman RANGEL. First, let me thank you for your patience, since I know you were here this morning.

We have a problem, and that is that everybody supports the objectives that Justice wants, and each time someone testifies for the administration or for Senator Nunn's bill, the objectives are said to be to get after drug traffickers, organized crime, white collar crimes and all of the things that we are against. But when we ask the specific questions as to what has impeded you under existing law, then we hear that Justice has perceptions that the law is too cumbersome.

If you read the General Accounting Office report carefully, it supports you in part, but it goes on to say that the laws are being used very effectively by certain districts. Further, the present Commissioner claims that over half of the cases, half the requests, come from seven U.S. attorneys. So there is conflicting testimony from the administration concerning to whether or not existing law is being properly and fully used.

---

[49] 750 in fiscal year 1975 to 932 in fiscal year 1980.

[50] 620 Strike Force cases initiated by IRS in fiscal year 1974 and 248 in fiscal year 1981.

I think you were saying in your testimony that even you couldn't determine whether or not a narcotics case could have been successfully prosecuted or even an indictment obtained because there are many factors that come together in an investigation and IRS is just one of them. Then, again, IRS does not even know what you would want, and if the record cannot be made that you even requested the information that they may have, and they will go on record saying they have not turned down any request even though they admit that not that many have been made. So while we all want to apprehend all of these criminals, it is still difficult for us to see how a tax collecting agency will not be adversely affected by the closer it gets to being an integral part of law enforcement. We have not been shown otherwise.

I assume you heard some of the testimony, that this is supposed to be the greatest tax system in the world and everyone envies it. If we have to do violence to it in order to bring about a better balance in what the American people really want, I would hope that we could make a better case than has been made by Justice this afternoon; that is, one that would be more consistent with the statements of the Internal Revenue Service and the General Accounting Office.

I don't see how there would be competing forces between the Treasury Department and Justice Department.

Mr. SCHMULTS. One point: First, the position I am stating today is not just the position of the Justice Department. This is an administration position; we are speaking with one voice.

I don't believe the IRS is saying anything any different. They are in favor of the bill, which is the administration bill referred to in my testimony. This is the administration speaking with one voice and the Treasury Department and IRS are in favor of the bill to which I have referred today and which has been introduced in the Senate.

Commissioner Egger has testified in favor of that bill before a Senate subcommittee, so we are speaking with one voice and I am not speaking for just the Justice Department but for the administration.

Two, our bill, Mr. Chairman, and we think this is a very important point, does not do any violence whatsoever to the Tax Reform Act. Indeed, I spent 2 years in the Treasury Department, first as General Counsel, later as Under Secretary, at a time when the Tax Reform Act was being considered.

I think I am very sensitive to, and totally support, our voluntary tax compliance system. It is a very important system we have in this country.

Chairman RANGEL. Are you talking about Senator Nunn's bill?

Mr. SCHUMLTS. No, I mean the administration bill, which is very close to the Senator's bill and which the IRS is supporting, and indeed the entire administration is supporting.

We would not do any violence to the protection and the confidentiality afforded taxpayers. In the very sensitive area of tax return information, for example, our bill still requires that a Federal prosecutor go to court and convince a court that the taxpayer information is relevant to a suspected Federal crime.

What we are doing is seeking to rationalize the requirements in the showing that must be made under the statute with what Federal judges are actually doing.

The statute provides a catch 22 now in that the Federal prosecutor has to prove that the taxpayer information contains probative evidence before he has even had a chance to see it. That is an absurd requirement in the existing law. Judges have not followed it and, as part of our bill, we would conform the law to what the judges have said.

Two, and this ties into why there have not been a lot of requests by some U.S. attorney out there. What we have now is a U.S. attorney, a Presidential appointee, in many cases running a large office, finds that he has a need for taxpayer information to make a nontax criminal case, be it drugs or organized crime up in New York, let's say, the application to the court now has to be prepared in New York. It then must be sent to the Department of Justice, must be signed by an assistant attorney general and finally go back to New York where it is presented to the district court there.

We see that as being part of the cumbersome procedures now in the Tax Reform Act that really ought to be changed. Such a change does not drive a big loophole or open wider doors in the act.

We think we have carefully constructed our proposal.

Chairman RANGEL. Have you heard the testimony that some U.S. attorneys officers have used existing law in getting convictions?

Mr. SCHMULTS. Yes, sir, but by and large, those are U.S. attorneys in charge of large offices.

What we find is that the small offices, and most of our U.S. attorney offices are small offices, don't have the time to keep up to date, to master the procedures, don't want to wait for the application to come in from Nebraska to Washington, D.C. We think that the cumbersome process is cutting down requests for taxpayer information and hurting criminal prosecutions.

Chairman RANGEL. It is a catch 22 as well, because we will never know how many times you would have been turned down if you had bothered to try to use the law. I think what you are saying is that the bureaucracy and the law are so cumbersome that the U.S. attorneys don't even bother to use it, and so if we relaxed it, liberalized it, then perhaps we would get a better understanding of what they could do.

We don't know how many cases you have lost or how many you could have made, how many times you would have been turned down, and the judges, I assume from most of the testimony we are hearing, are violating the law because they are not interpreting it strictly but rather loosely.

Mr. SCHMULTS. They are interpreting it in a way that makes sense.

Chairman RANGEL. You have a problem with it, not us.

Mr. SCHMULTS. That creates more complexity and confusion, because when people look at the law, particularly if you are not an experienced prosecutor in a large city, you may not know how judges are in fact interpreting the law.

You can look this up but these are very busy people; the essential point is where you can eliminate complexity and cumbersome procedures and not injure in any way taxpayer privacy you should do so. In the return area under our bill you still have to go to a court. Quite frankly, Mr. Chairman, we do not see what will be lost in the area of taxpayer privacy by our bill.

We see very substantial gains in the area of criminal justice.

Chairman RANGEL. We all want the same objective. I am just asking whether you can make a better case as to why existing law has not worked and why there should be changes.

Mr. SCHMULTS. In my long statement I have about 14 or 15 points which I think when you go through you will find do make a good case for a change in the law.,

Chairman RANGEL. Senator Nunn has any number of points in his testimony.

His staff has attempted to establish that existing law has been an impediment to successful prosecutions. It is easy enough to change the law if necessary.

But we have to have some assurances that legislative changes will produce the effect we want or that existing law has been an impediment to it. You see, the Senate didn't have all of those hearings when they passed the Nunn amendment and we got the darn thing in an economic recovery package, and the bill looked just as bad as the economic recovery package. That's why we are here today.

Mr. SCHMULTS. The Senate has had hearings now on the bill, and so we hope that we will have hearings on our bill in the House.

Chairman RANGEL. OK. Well, most of the witnesses look at me and they say, you understand the narcotic problem just as well as anyone else, therefore, I do hope we will receive some information that that would convince members of the committee that the changes the administration wants are in fact necessary. Actually, I don't see how the proposed changes will help. Therefore, you could help us in telling us exactly how you think changes are going to help.

Mr. SCHMULTS. Yes, but I do want to remind you that the IRS is supportive and totally on board and the administration is speaking with one voice on this bill and that is in favor of it.

Chairman RANGEL. OK, but they talk in different tones. The Commissioner was here talking about all the cooperation and successful joint ventures he was having with DEA. It was hard for me to get the impression that he wanted others to have more access to his tax files, but I probably missed that.

We will be able to bring those voices together and I do hope that you are able to assist us to see how it is going to help the Nation's crime problems. Each time we use drug trafficking, you realize you pick up the votes of every Member of the House and Senate.

It is so easy to say that these traffickers are going free because of our stubborn insistence on keeping the rigidity of the privacy laws. If we are going to change them and not adversely affect privacy and cause Justice to be more successful, this is what we want.

True, I have not read your statement, but we will study the statement; but more importantly, I hope that our staffs can get together and make the case for members of the committee formally or informally, rather than be restricted to the hearing process, so when we go to the full committee it won't be a proadministration or antiadministration position, rather, we would be improving the law.

Mr. SCHMULTS. We stand ready to give you all the assistance we can in any way that we can or you would wish it.

Chairman RANGEL. I guess if the DEA and the IRS and Justice got together, we could clearly find out what the administration position is.

Mr. Schmults.

Mr. SCHMULTS. Yes, the administration position is reflected in the bill and in my testimony before the Senate committee, my longer written statement here and testimony on the specific bill before the Ways and Means Committee.

Chairman RANGEL. I was even getting the impression that the administration's proposal might be costly. The IRS would need additional personnel.

Mr. SCHMULTS. No, sir, there will be no additional burden on the IRS whatsoever. With some 88,000 people, we think they will be able to turn over to the Department of Justice information which they become aware of. It requires no additional investigations, review of documents, or anything else on their part, so we see no additional burden other than some modest Xeroxing costs.

Chairman RANGEL. They were familiar with tax-related crimes but not familiar with unrelated tax crimes.

Mr. SCHMULTS. Not so. It does not require them to hire one additional person or take a look at one single document.

Chairman RANGEL. OK, we will get together with the Commissioner, because he is getting together figures for us. Thank you very much for your patience.

I look forward to working with you on this.

OK, we will recess for 10 minutes and then we will come back.

[Brief recess for vote.]

Chairman RANGEL. The committee will reconvene, and we have the American Bar Association, Section of Taxation, Mr. John Nolan and Mr. John B. Jones, Jr., the vice chairman of government relations. And thank you for your patience, and your full statement will appear in the record.

STATEMENT OF JOHN S. NOLAN, CHAIRMAN, SECTION OF TAXATION, AMERICAN BAR ASSOCIATION, ACCOMPANIED BY JOHN B. JONES, JR., VICE CHAIRMAN, GOVERNMENT RELATIONS

Mr. NOLAN. The Section of Taxation of the American Bar Association is an organization of 25,000 tax lawyers throughout the United States. We are joined in this statement by the Section of Individual Rights and Responsibilities of the Association. We speak only for the two sections, however; we do not speak for the entire American Bar Association. I will make a few major points.

We are deeply concerned as to the impact of the administration bill on voluntary compliance and on the self-assessment system. There are changes that could be made in existing law to aid law enforcement agencies without compromising the essential confidentiality of tax returns and taxpayer return information, but we think the administration's bill goes too far.

In 1976, we stated our strong opposition to unlimited disclosure of returns and return information for nontax administrative or judicial proceedings. Congress at that time determined that the law did not afford citizens the degree of privacy to which they were entitled. As a result, the Tax Reform Act of 1976 amended section 6103 to require a Federal agency to obtain an ex parte court order from a Federal district judge for disclosure of tax returns and other tax information obtained from the taxpayer or his representative for use in nontax investigations and proceedings. In all major respects, the Tax Reform Act of 1976 struck a proper balance between the need to investigate and prosecute nontax crime and taxpayer privacy rights. Some of the changes under consideration could upset the proper balancing of these interests. Our greatest concern is that the requirement for a court order to obtain taxpayer return information would be eliminated in the case of taxpayers other than an individual or a business of two individuals.

We oppose any such distinction between individuals and other taxpayers. Despite the fact that corporations and other entities do not enjoy the protection of the fifth amendment, such taxpayers are entitled to privacy and confidentiality for all tax information they are required by law to submit to the Internal Revenue Service. The Supreme Court in its recent Upjohn decision upheld the attorney-client privilege for corporations as well as individuals. Much of the same reasoning applies here.

Tax information submitted by business taxpayers normally includes a substantial amount of confidential commercial and financial data. In addition, a company's tax information, frequently information about individual officers and other employees. Compliance under our voluntary tax assessment system might suffer materially if the confidentiality of return information is reduced for corporations and other nonindividual entities required to furnish tax information. If a corporation's tax books and records are available to the Justice Department and U.S. attorneys merely for the asking because a nontax investigation is in progress, some businesses may be tempted to maintain less complete books and records. In addition, the choice of form of business organization of smaller businesses might be distorted in order to obtain the broader protection.

Moreover, corporate taxpayers may be less cooperative in submitting tax information requested during an audit examination, requiring the Service to issue an administrative summons or prove in a summons enforcement action the relevancy of the information requested and the fact that it is not already in the Service's possession. Quite clearly, substantial inroads on taxpayers' privacy would significantly slow the Service's examination process and, absent funds for additional revenue agents, further reduce the Service's audit coverage of taxpayers generally—possibly encouraging more taxpayers to "play the audit lottery."

Consequently, we urge that Congress reject any proposal to reduce the confidentiality accorded to taxpayers return information of nonindividual taxpayers.

On other points we would agree with General Schmults that the standards for issuing the court order could be changed to conform to what the courts are actually doing. Present law should be amended to delete or substantially modify the requirement for a finding that either the information can be reasonably obtained from any other source, or that the tax information is the most probative evidence in the matter. That standard is virtually impossible to satisfy in actual practice, and it should be deleted.

We also believe, Mr. Chairman, that the procedures in present law whereby the Internal Revenue Service may disclose so-called "return information" other than taxpayer return information that may constitute evidence of a Federal crime reflect the correct balance of competing considerations. We oppose the administration proposal to require the Internal Revenue Service to disclose such information in the case of entities consisting of more than two individuals "if there is reasonable cause to believe such entity was formed or is being operated or maintained with a purpose of facilitating or engaging in Federal criminal activity." A mandatory rule would require the Service either to divert resources to ascertain whether a crime exists or to refer every case where any possibility of crime exists.

We agree that the provisions of present law should be broadened to permit U.S. attorneys to seek returns and tax information and to permit District Directors to disclose returns and tax information, but we oppose any broader delegation of authority.

In connection with nontax related law enforcement, we recommend that information, including a taxpayer's address and social security number and whether he has filed a tax return for any year, be disclosed only on court order, as under current law.

We oppose the redisclosure of returns and taxpayer return information to State law enforcement officials, recommending instead that disclosure remain limited as under current law.

We oppose the proposal to state that section 6103(i) does not preclude joint investigations by the Service. We feel that is an open opportunity to circumvent the existing law with respect to confidentiality.

We have substantial concerns about the proposal to disclose taxpayers' return information to foreign intelligence or counterintelligence personnel.

We support the disclosure of taxpayer return information and other return information to competent authorities of foreign governments but only pursuant to treaty or convention and after judicial review.

Thank you.

Those are the main points that we have made in our full statement, Mr. Chairman. Our statement deals in some length with these, including our reasoning, and we ask the committee to consult that statement.

[The prepared statement follows:]

Statement of John S. Nolan, Chairman, Section of Taxation, American Bar Association, on Behalf of the Section of Taxation and the Section on Individual Rights and Responsibilities

INTRODUCTION

The Section of Taxation of the American Bar Association is an organization of 25,000 tax lawyers throughout the United States. We are joined in this Statement by the Section of Individual Rights and Responsibilities of the Association. We have studied the important issue of confidentiality of tax returns and tax return information for many years. We speak only for the two Sections, however; the American Bar Association itself has not considered these matters through its governing bodies.

I. SUMMARY

We strongly support the protection of important privacy rights of taxpayers now contained in Section 6103(i) of the Internal Revenue Code. Voluntary compliance with our tax system is encouraged by those statutory guarantees of confidentiality. Without such assurances of confidentiality, we believe the self assessment tax system would suffer. There are changes which could be made in Section 6103(i), however, which may assist law enforcement agencies consistent with preserving the confidentiality of tax returns and taxpayer return information. Some of these changes are proposed in S. 732 and in the Administration's proposals submitted on November 19, 1981, now set forth in S. 1891.

Section 6103(i) is not a time-weary provision ready for a major overhaul. It was enacted only a few years ago as part of the Tax Reform Act of 1976. At that time after extensive consideration of the facts and issues, Congress acted strongly to protect the confidentiality of tax returns and taxpayer return information. This was not done to make it difficult for law enforcement officials to detect and prosecute criminals. Rather, Congress then acted to protect legitimate rights of privacy and to strengthen compliance with the tax laws by self-assessment. We believe the basic balance of competing interests which Congress struck in 1976 is sound today. It certainly should not be shifted without a strong factual showing of need.

The essential issues are: (1) whether independent judicial review of requests to disclose tax returns and taxpayer return information should continue to be required; and (2) whether the confidentiality of tax returns and (2) whether the confidentiality of tax returns and taxpayer return information of entities consisting of more than two individuals should be maintained. We are convinced as to these two essential issues that no changes should be made.

In addition to these two basic issues, other questions have been raised. Our positions on these issues are as follows:

1. We agree, that a court order authorizing disclosure could be issued by either a Federal district judge or a United States magistrate. Moreover, we agree that the scope of such an order could properly include tax returns, taxpayer return information, and other return information.

2. The Section of Taxation agrees that the standard of review for court-ordered disclosure of returns and taxpayer return information should be changed to reflect the manner in which the standard is being applied by the courts. The Section of Taxation also agrees that disclosure may be ordered by a court to locate a person who is a fugitive from justice and for whom a judicial arrest warrant has been issued. The Section of Individual Rights and Responsibilities takes no position on these matters.

3. We do not believe that the proposals to adopt new definitions of "return information", "nonreturn information" or "investigative return information" and "investigative nonreturn information", either generally or as limited to section 6103(i), offer any clear improvement over the present statutory definitions, which are well understood by courts, the IRS and other agencies, and by taxpayers and their advisors.

4. We believe that the procedures in present law relating to the Service's disclosure of return information other than taxpayer return information that may constitute evidence of a federal crime draw the correct balance between competing considerations. A mandatory rule would require the Service either to divert resources to ascertain whether a crime exists or to refer every case where any possibility of crime exists.

5. We agree with proposals for emergency disclosure upon an expedited basis pursuant to the standards of the Right to Financial Privacy Act of 1978 (12 U.S.C. 3414(a)) to avoid threats to life, serious property damage, or flight from prosecution. It should be made clear, however, that the strict standards for emergency disclosure should not be ameliorated in practice.

6. We agree that the provisions of present law should be broadened to permit U.S. Attorneys to seek returns and tax information and to permit District Directors to disclose returns and tax information.

7. We recommend retention of the provisions of present law imposing a monetary penalty upon an Internal Revenue Service employee who discloses tax information protected from disclosure. We recommend the imposition of a monetary penalty on a federal government employee who receives such improperly disclosed information.

We agree, however, that there should be provision for an affirmative good faith defense against such penalties.

8. In connection with non-tax related law enforcement, we recommend that information, including a taxpayer's address and social security number and whether he has filed a tax return for any year, be disclosed only on court order, as under current law.

9. We oppose the re-disclosure of returns and taxpayer return information to state law enforcement officials, recommending instead that disclosure remain limited as under current law.

10. We oppose the proposal to state that Section 6103(i) does not preclude joint investigations by the Service.

11. We have substantial concerns about the proposal to disclose taxpayer return information to foreign intelligence or counter intelligence personnel.

12. We support the disclosure of taxpayer return information and other return information to compentent authorities of foreign governments but only pursuant to treaty or convention and after judicial review.

II. DISCUSSION

In general, we support new initiatives by the Federal Government to investigate and prosecute non-tax crimes forcefully and effectively. In our view, there are changes which would improve the government's investigative and prosecutorial operations. We are deeply concerned, however, that the legitimate privacy interest of taxpayers be protected, both as a matter of civil rights and preservation of the integrity of our self-assessment tax system. The Tax Reform Act of 1976 attempted to strike a balance between the need to investigate and prosecute non-tax crime and taxpayer privacy rights. Some of the changes under consideration could upset the proper balancing of these interests. The major objective of these proposals may be achieved, however, without significantly reducing taxpayer privacy.

Prior to the amendments to Section 6103 adopted in the Tax Reform Act of 1976, a Justice Department attorney or U.S. Attorney was able to obtain tax information from the Service whenever "necessary in the performance of his official duties". A written application, signed by the Attorney General, Deputy Attorney General, an Assistant Attorney General, or the U.S. Attorney involved in the case was required. As a practical matter, Justice Department attorneys and U.S. Attorneys obtained requested tax information at their own discretion, inasmuch as there were no standards for or restrictions on disclosure of this kind of information.

In 1976, we stated our opposition to unlimited disclosure of returns and return information for non-tax administrative or judicial proceedings. Congress determined that pre-1976 law did not afford citizens the degree of privacy to which they were entitled. As a result, the Tax Reform Act of 1976 amended Section 6103 to require a federal agency to obtain an ex parte court order from a federal district judge for disclosure of tax returns and other tax information obtained from the taxpayer or his representative for use in non-tax investigations and proceedings. Under present law, a court order is not necessary to obtain disclosure of tax information received from third parties.

The 1976 legislation represented a compromise of the efforts of government agencies to investigate and prosecute illegal activities and the substantive rights of privacy and confidentiality of taxpayers in general. The Senate Report explained that there was a substantial question whether actual and potential disclosures of tax returns and return information to other federal and state agencies denied to American citizens their reasonable expectation of privacy in regard to such information. See S. Rep. No. 938 at 317. There was an equally substantial question whether the public's reaction to a perceived abuse of privacy would impair the effectiveness of this country's "very successful voluntary assessment system." Id. Another more general concern was whether tax returns and tax information should ever be used for any purposes other than tax administration. Id. The 1976 Tax Reform Act has been described as a broad consensus as to the appropriate degree of intrusion of taxpayers' privacy in aid of non-tax law enforcement. See Parnell, "The Right to Privacy and the Administration of the General Tax Laws," 31 Tax Lawyer 113 (1977).

The Internal Revenue Code not only requires taxpayers to file tax returns, but also requires them to maintain books and records adequate to prove their tax liabilities. Under the three-part definitions of present law, (tax "returns", "taxpayer return information" and "return information") a court order is required before tax returns, information from tax returns, or other information obtained from the taxpayer or his representative may be disclosed. Taxpayers are entitled to a high degree of privacy for tax returns and tax information obtained from them or their representatives and supplied to the Service to support the tax return. Moreover, American taxpayers' expectation of privacy is a significant factor in preserving the effective operation of our self-assessment system. Any erosion of this privacy right, at a time when taxpayer compliance already is under great pressure, would adversely affect taxpayers' willingness to comply with tax reporting requirements and voluntarily to supply, directly or through a representative, tax information to the Internal Revenue Service.

Court order requirement

We urge the requirement that a court order be obtained for disclosure of a taxpayer's tax return, and any tax information obtained from the taxpayer or his representative, be retained. We would agree, however, that such an order could be properly issued by United States magistrates as well as Federal district judges.

Present Section 6103(i)(1) provides that before a court will issue a disclosure order there must be reasonable cause to believe (1) that a specific criminal act has been committed; (2) that the return or return information is probative evidence of a matter in issue related to the commission of the criminal act; and (3) that either the information cannot reasonably be obtained from any other source, or that tax information is the most probative evidence of the matter in issue.

The courts have considered the third standard of present Section 6103(i)(1) to be virtually impossible to satisfy. Consequently, we agree that the third standard be modified or deleted.

Individual taxpayers and business taxpayers

Both S. 732 and the Administration proposal would essentially retain present disclosure law as to individual taxpayers, but they would permit more extensive disclosure with respect to other taxpayers. Under such proposals, a Justice Department attorney or U.S. Attorney would be required to obtain a court order for the disclosure of tax returns or any other tax information obtained from an individual taxpayer or his representative, or a business of two individuals, but would not need to obtain a court order with respect to other taxpayers for information beyond the return itself.

We oppose any such distinction between individuals and other taxpayers. Despite the fact that corporations and other entities do not enjoy the protection of the Fifth Amendment, such taxpayers are entitled to privacy and confidentiality for all tax information they are required by law to submit to the Internal Revenue Service. The Supreme Court in its recent *Upjohn* decision upheld the attorney-client privilege for corporations as well as individuals. Much the same reasoning applies here.

Tax information submitted by business taxpayers normally includes a substantial amount of confidential commerical and financial data. In addition, a company's tax information frequently includes personal information about individual officers and other employees.

Compliance under our voluntary tax assessment system might suffer materially if the confidentially of return information is reduced for corporations and other non-individual entities required to furnish tax information. If a corporation's tax books and records are available to the Justice Department and U.S. Attorneys merely for the asking because a non-tax investigation is in progress, some businesses may be tempted to maintain less complete books and records. In addition, the choice of form of business organization of smaller businesses might be distorted to obtain the broader protection.

Moreover, corporate taxpayers may be less cooperative in submitting tax information requested during an audit examination, requiring the Service to issue an administrative summons or prove in a summons enforcement action the relevancy of the information requested and the fact that it is not already in the Service's possession. Quite clearly, substantial inroads on taxpayers' privacy would significantly slow the Service's examination process and, absent funds for additional agents, further reduce the Service's audit coverage of taxpayers generally—possibly encouraging more taxpayers to "play the audit lottery". Consequently, we urge that Congress reject any proposal to reduce the confidentiality accorded to taxpayer return information of non-individual taxpayers.

Mandatory requirement of disclosure

Section 6103(i)(3) now provides that the Service may disclose return information that may constitute evidence of a violation of federal criminal laws to apprise the head of the appropriate federal agency of the possible commission of a crime. The area of permissible disclosure includes only tax information obtained from persons other than the taxpayer or his representative. Both S. 732 and the Administration's proposal would make this requirement mandatory. We believe that present law imposes no restriction on the transfer of such information and that a mandatory requirement would impose severe burdens upon the Service.

The Administration proposal, S. 1891, would require disclosure of taxpayer return information of entities consisting of more than two individuals. This requirement would apply "if there is reasonable cause to believe such entity was formed or is being operated or maintained with a purpose of facilitating or engaging in Federal criminal activity." As previously stated, we strenuously object to providing different confidentiality standards for different categories of taxpayers. We are greatly concerned that the Administration's proposal permits unlimited discretion to make disclosure of business tax information.

If organized criminals establish a trust or corporation to sell narcotics, such an organization obviously falls within the Administration's proposal—its very purpose is to "facilitate" or "engage in" federal criminal activity. On the other hand, consider a large corporation with a substantial number of employees who have made illegal kickbacks or political contributions. Is it an entity "*maintained* with a purpose of facilitating or engaging in Federal criminal activity" (emphasis added)? We submit that there are an infinite variety of these distinctions, and the Internal Revenue Service is in no position to make these judgments. This burden should not be imposed upon the Service.

Moreover, this standard would require the Service to determine the applicability of all Federal non-tax criminal laws. That is not the responsibility of the Service and they cannot effectively make such determination. The agency or agencies responsible for enforcement of Federal non-tax criminal laws should make the determination whether an entity is engaged in non-tax Federal criminal activity. If they do, they can then obtain tax returns and taxpayer return information, as well as other tax information, by application for a court order. If the responsible agency is unable to make such a determination, the Service is not in a position to second-guess the responsible agency, or, indeed, to reach a determination contrary to that of the agency with primary jurisdiction.

Emergency disclosures

There are proposals in S. 732 and the Administration proposal which would require mandatory disclosure of returns and other tax information under emergency circumstances. Disclosure would be directly to the appropriate federal investigative agency charged with enforcing the applicable law, and it would encompass information necessary to apprise the agency of the emergency. We agree with these proposals, but we question the utility of a post-disclosure report or review unless there is an appropriate remedy for an improper emergency disclosure.

Delegation of authority to obtain disclosure

Present Sections 6103(1) (1) and (2) require that applications for court ordered-disclosure and requests for disclosure of tax information obtained from third parties must be made by agency heads or the Attorney General, Deputy Attorney General or an Assistant Attorney General. Until very recently, the practice of the Internal Revenue Service was that disclosure of requested returns and tax information, including information obtained from third parties, had to be approved in the National Office of the Service. Effective June 1, 1980, however, Delegation Order No. 156 (Rev. 1) was amended (Amendment 1, 45 Fed. Reg. 38199, June 6, 1980) to delegate the authority to disclose requested returns and tax information to additional officials of the Service, and more particularly to Service officials in the field.

If the present law has been unnecessarily cumbersome and time-consuming in centralizing requests for disclosure and in making disclosures, we urge that there not be overbroad delegation of authority for making requests and making disclosures. Within the Justice Department, the authority to make applications for a court order and requests for the disclosure of tax information should not, as provided in S. 732, go so far as "any other head of a Regional Office of the Department of Justice or a supervisory attorney specifically designated by the Attorney General".

Similarly, we recommend that within the Internal Revenue Service, the authority to disclose properly disclosable tax information, consistent with the Commissioner's amended Delegation Order No. 156, not include an Assistant Regional Commissioner in charge of the Criminal Investigation Division of the Internal Revenue Service or the chief of the Criminal Investigation Division of any local Internal Revenue Service Office.

Under our recommendations, authority could be delegated to United States Attorneys to apply for court-ordered disclosure, and disclosure could be made by District Directors. This would decentralize authority substantially. Further delegation or decentralization should not be permitted unless it is established that these procedures are unworkable. Moreover, at these levels there is a greater assurance of objective review of the need to obtain tax returns and taxpayer return information.

Disclosure to competent authority and foreign intelligence access

The Administration proposal, S. 1891, contains provisions to allow disclosure of return information and taxpayer return information of any taxpayer to a competent authority of a foreign country which has an appropriate treaty or convention with the United States. An ex parte court order would be required prior to disclosure. This broadens existing law by permitting disclosure in connection with non-tax crimes. We believe Senate ratification of such treaties or conventions and the requirement of a court order provide sufficient safeguards, and, accordingly, we agree with the proposed amendment.

S. 1891 also permits disclosure upon personal certification by the Attorney General to foreign intelligence personnel. There is a danger in such disclosures because there would be no court review and because the impetus for disclosure could be initiated by foreign intelligence personnel for purposes which we might classify as political purposes instead of proper law enforcement purposes. We are not aware of the need for such disclosures, nor do we have any information as to how frequent or extensive disclosures might be made under that authority.

Redisclosure to State officials

The Administration proposal would add a new section 6103(i)(7) authorizing Justice Department attorneys or United States Attorneys to whom disclosure of tax information has been made and who possess information which is relevant to the violation of a state felony statute to apply to a federal district court for an ex parte order to disclose the information to a state law enforcement official. Although we strongly support federal law enforcement efforts, in our view the privacy and confidentiality of tax returns and tax information also are important federal interests. There is no justification for redisclosures to state law enforcement officials in connection with felonies charged under state law. Taxpayers' rights of privacy and confidentiality clearly should prevail in these situations. Accordingly, we oppose the proposal to permit redisclosure of information to state authorities.

Use in judicial or administrative proceeding

The Administration proposal would make it clear that return information and taxpayer return information of any taxpayer which was properly disclosed pursuant to court order, or otherwise in conformity with Section 6103(i), could be introduced as evidence in accordance with existing rules and law. Such information could be disclosed as required by the Jencks Act or other discovery requirements. We agree with that proposal.

Joint investigations

The proposal in S. 1891 to state that nothing in Section 6103(i) precludes the Service from working jointly with another federal agency in a joint investigation of tax and non-tax crimes is of serious concern. This provision could be used as a means to disregard the protections of confidentiality contained in Section 6103(i). Unless carefully determined limits are placed upon the manner in which such joint investigations may be initiated, we oppose this proposal.

Good faith exceptions for unauthorized disclosure

Section 7213 states it is a felony to make an unauthorized disclosure of a tax return or tax return information. S. 732 and S. 1891 would provide an affirmative defense to prosecution under that section if the disclosure resulted from a good faith, but erroneous, interpretation of Section 6103 while a federal employee was acting within the scope of his employment duties. We agree with this proposal.

Section 7217 presently provides that civil damages may be obtained from a government employee and be awarded to a taxpayer for unauthorized disclosure of his return or return information. S. 732 and S. 1891 would provide that such damages will be paid by the federal government, rather than the government employee. We support that provision, provided that the employee would also be personally liable if the improper disclosure was willful, corrupt, malicious or for money. The possibility that substantial civil damages could be imposed on Internal Revenue Service employees may in some instances have made them overly cautious when asked to disclose tax information.

While it may be that the affirmative defense may already be in practical operation by court interpretation of existing law, we agree that the standard should be enacted to assure that result.

Penalties upon recipients

Where there is an illegal disclosure of tax information, there are always two parties involved—the one who discloses and the one who receives the disclosed information. Where they are both government employees, we submit that they should both be liable for penalties and civil damages. Accountability of the government employee-receiver of the illegal disclosure would assure against his exerting undue pressure for the disclosure.

A jail sentence, however, is not a necessary penalty on either the giver or the receiver of an unauthorized disclosure. It might indeed cause Service and other government employees to be overly cautious. A criminal fine would be adequate.

Disclosure of taxpayer identity

Present Section 6103(b(6) defines the term "taxpayer identity" as the taxpayer's name, address and social security number. In connection with non-tax law enforcement, current law generally applies the court order requirement to any item of "taxpayer identity", although disclosure of information obtained from third parties under Sections 6103(i) (2) and (3) may include the taxpayer's name and address.

We submit that the current law as to disclosure of "taxpayer identity" in connection with non-tax law enforcement is correct. The 1976 Tax Reform Act, which was the product of much discussion and compromise in this respect, deleted a rule of unlimited disclosure from the law. We recommend that the present court order requirement be retained as to identifying information. Accordingly, we oppose the disclosure of any information related to a taxpayer's name, address, Social Security number and filing status upon the mere written request of a Justice Department attorney in connection with non-tax law enforcement.

CONCLUSION

Although we strongly support federal law enforcement efforts, we believe equally as strongly that the privacy and confidentiality of tax returns and tax information are an important federal interest. The Tax Reform Act of 1976 generally struck a reasonable balance between the sometimes competing needs for confidentiality of tax information and effective federal law enforcement. We agree that some further refinements are necessary to achieve a more appropriate balance. We do not feel, however, that there is adequate justification for re-disclosures to either state law enforcement officials in connection with felonies charged under state law, or to federal officials in connection with litigation on federal civil claims. Taxpayers' rights of privacy and confidentiality should prevail in these situations to maintain the proper balance.

Chairman RANGEL. Thank you, Mr. Nolan.

The thrust of the Bar Association's statement on page 3 is concerned with the rights of privacy of individual taxpayers?

Mr. NOLAN. That is our main point. We feel that the balance that was struck in the 1976 act whereby an ex parte court order is required should apply as much to business taxpayers as to individual taxpayers. That is not an unreasonable burden to impose upon the Government. We feel that the testimony today indicates quite clearly that the court order process is a very viable procedure and could be extended by further education of those U.S. attorneys who are not adequately using it, and we see no reason for weakening that protection of taxpayer confidentiality. If you do so, you will disturb the audit processes in a severe way, and we think risk a decrease in the level of voluntary compliance.

Chairman RANGEL. I don't see that in your statement. Is that here?

Mr. NOLAN. Yes, we have made that point.

Chairman RANGEL. I thought you were trying to get the nonindividual——

Mr. JONES. Pages 9 and 10, Congressman.

Chairman RANGEL. Individual tax base and business tax base?

Mr. NOLAN. Thank you. Yes.

Chairman RANGEL. Thank you for your contribution.

Mr. Cohen has been rather patient with us today from the Chamber of Commerce of the United States, chairman of the taxation committee, member of the board of directors.

STATEMENT OF EDWIN S. COHEN, CHAIRMAN OF THE TAXATION COMMITTEE, MEMBER OF THE BOARD OF DIRECTORS, CHAMBER OF COMMERCE OF THE UNITED STATES, ACCOMPANIED BY DAVID E. FRANASIAK, DIRECTOR OF THE CHAMBER'S TAX POLICY CENTER

Mr. COHEN. Thank you, Mr. Chairman.

I am Edwin S. Cohen. I am a member of the board of directors and chairman of the taxation committee of the chamber of commerce, and a partner in the law firm of Covington & Burling, of Washington, D.C.

I am accompanied by Mr. David E. Franasiak, director of the chamber's tax policy center.

On behalf of the chamber's more than 200,000 businesses and associations and local State chamber members, we welcome the opportunity to present to you our views on the general issues relating to disclosure by the IRS and tax information to other agencies of the Government for administration of Federal laws not relating to tax administration.

Under the present section 6130(i)(1), the information given by taxpayer to the IRS during the course of a tax audit may not be disclosed by the IRS to other Government agencies without Federal court order.

S. 732, Senator Nunn's bill, and S. 1891, which is the administration bill referred to by Deputy Attorney General Schmults earlier, both of which are now pending in the Senate, would eliminate the need for a court order in many instances, and would expand the right of other agencies to obtain information that is now routinely made available by taxpayers to the IRS during the course of tax audits.

The chamber believes the proposed changes would pose significant problems for businesses with more than two owners, particularly for smaller firms. We, therefore, join with Mr. Nolan, who testified on behalf of the tax section of the American Bar Association in his opposition to this change.

Our particular reasons for this on behalf of business relate in part to the practices of large companies, and in part to the practices of small companies undergoing tax audits by the IRS.

Large companies are continually under audit by the IRS and the companies maintain a staff of tax employees who constantly provide the IRS personnel with financial and operating data relating to the taxable years that are under review.

Those larger companies do not as a rule forward this material that they plan to disclose to the IRS to their general counsel's office prior to the disclosure.

Our concern is that for these larger companies, under these two bills, businesses necessarily would be hesitant about furnishing information to IRS agents without review by legal counsel familiar with the nontax Federal laws that impose criminal sanctions on businesses.

The bills would permit a Federal agency official having jurisdiction over enforcement of any of those nontax laws, who may be considering whether the customers or suppliers may have violated a Federal law having criminal sanction, to obtain from the IRS on his own written request all of the firm's underlying tax return information, including books and records gathered during the course of an IRS audit.

I need not remind you, Mr. Chairman, of the many Federal laws that regulate businesses and contain Federal criminal sanctions. These would include, for example, the Occupational Safety and Health Act, the antitrust laws, the Foreign Corrupt Practices Act, the securities laws, consumer product safety laws, and environmental laws, antitrust laws, et cetera.

The interpretation and application of those laws are often uncertain. Now, the proponents of the bills point to the need for more effective means of combatting organized crime, drug trafficking and the like, and in similar major criminal ventures that confront our society. The chamber and its many members heartily support major efforts to stamp out these evil forces but these bills, Mr. Chairman, are unnecessarily broad, and would authorize disclosure of tax information by the Service to other Government agencies seeking to investigate possible violations of a host of business regulatory statutes having no relationship whatsoever to organized crime or drug trafficking and the like.

I do not want to indicate that the Department of Justice or other proponents of the bill would intend to use the proposed statute in this fashion, but the possibility of that use should be foreclosed in the statute itself in order that businesses may continue to supply information to the IRS in the course of tax audits without concern that it might be so abused.

I referred also to smaller firms, and we think that they would be disproportionately affected by these bills. When the smaller firms are audited, they tend to rely on an accountant to explain the information to the IRS during the course of the tax audit. Lawyers are not customarily involved in the audit, unless and until a tax dispute arises and develops as a result of the audit.

Under these pending bills, these smaller businesses would be hesitant about supplying information to the IRS without review by a lawyer having knowledge of nontax Federal statutes which affect that industry and which contain criminal sanctions.

We have a very real concern that this additional burden placed on the already overburdened small business sector would impair the maintenance of the strong and healthy small business community.

Moreover, as Mr. Nolan mentioned and others have mentioned, under the bills the IRS would be required on its own initiative to disclose to other agencies information obtained under a tax audit if the information may constitute evidence of a violation of a Federal criminal law that the other agency enforces.

The IRS agents are not trained to be familiar with the many nontax Federal laws that contain criminal sanctions, nor to analyze information to determine whether it "may constitute" evidence of a violation of any of those laws. Thus neither the agents nor the taxpayers would know during the course of the audit whether the IRS on its own initiative would have to disclose the information to the Department of Justice or to other Federal agencies for consideration under those many nontax Federal laws.

We, therefore, believe that such a requirement would impose a most serious burden of decision and review both on the IRS and the business taxpayers and would delay and hamper the administration of the tax laws.

Mr. Chairman, the Chamber strongly supports the goals of these bills to provide the nation with greater protection from organized crime, but we do object to the unnecessary breadth of the proposals and believe that they should be substantially modified before they are enacted.

Those modifications, we think, should insure that taxpayers need not be concerned that papers and data routinely and voluntarily furnished during an IRS audit may end up without a court order in the hands of other agencies of the Government for use under various regulatory statutes having criminal sanctions.

I may add one thought, Mr. Chairman, that occurred to me as I sat and listened to some of the testimony. It seemed to me that maybe the reason why these bills have produced this problem is because under existing law the heads of other Federal agencies and the Justice Department alike must secure court orders to obtain the information.

The Justice Department wishes to be able to obtain the information without court order. I am inclined to agree with Mr. Nolan and the bar association, that the court order requirement should be retained, but even if it were to be waived in the case of major crimes being investigated by the Justice Department, that is no reason to carry along with the Justice Department the permission for the heads of other Federal agencies to secure like information without a court order.

I think it is just being done because the statute is drafted in that fashion now, and if the Justice Department feels this need, it feels that the simplest amendment is to give that increased right to the other Federal agencies as well. It is to that latter exclusion that we most strenuously object.

[The prepared statement follows:]

STATEMENT OF EDWIN S. COHEN, CHAMBER OF COMMERCE OF THE UNITED STATES

My name is Edwin S. Cohen. I am a member of the Board of Directors and Chairman of the Taxation Committee of the Chamber of Commerce of the United States, on whose behalf I am appearing today. I am a member of the law firm of Covington & Burling, of Washington, D.C., and I am accompanied today by David E. Franasiak, Director of the Chamber's Tax Policy Center.

On behalf of the Chamber's over 200,000 business, trade association, and local and state chamber members, we welcome this opportunity to present our views on the general issues involved in the present section 6103(i) of the Internal Revenue Code relating to disclosure by the Internal Revenue Service of tax information to other agencies for administration of federal laws not relating to tax administration. There are bills now pending in the Senate to amend that provision, one being S. 732, introduced March 17, 1981 by Senator Nunn and others, and the second being S. 1891, introduced November 24, 1981 by Senator Roth and others and embodying, I understand, proposals by the Administration.

S. 732 was approved by the Senate on July 27, 1981 as an amendment to the Economic Recovery Tax Act of 1981. It was deleted from the new tax bill in conference, with the understanding that hearings on the proposals would be held.

SUMMARY

Although we strongly support the goal of S. 732 and S. 1891 to strengthen the government's ability to combat narcotics traffickers and organized crime, we strongly oppose the broad proposals for disclosure of tax information set forth by the bill. If enacted, S. 732 and S. 1891 would allow other government agencies, without court order, to have unwarranted access to business records and information now routinely made available by taxpayers to the Internal Revenue Service in connection with tax audits. Indeed, S. 732 would require the I.R.S. on its own initiative to disclose to other government agencies any such information that "may constitute" evidence of a violation of any federal criminal law, and would permit persons in the other agency in turn to disclose the information to other federal government personnel or witnesses; S. 1891 would limit this requirement to some extent.

The possibility of such disclosure, without judicial permission, regarding possible violation of any of the many federal laws having criminal sanctions will make businesses hesitant about furnishing information to the I.R.S. because of concern that it might initiate or affect non-tax investigations or actions by other agencies. Lawyers for taxpayers may have to review such information prior to disclosure to the I.R.S. because of possible collateral effect on non-tax matters. This would tend to delay or inhibit the disposition of tax audits and increase the expense of those audits to taxpayers. While the bills would affect all businesses with more than two individual owners, they would impose a special burden on small businesses that do not customarily have lawyers involved in tax audits unless and until a disagreement develops between the I.R.S. and the taxpayer.

ANALYSIS

Under present Section 6103(i)(1), information given by a taxpayer to the I.R.S. during the course of a tax audit may not be disclosed by the I.R.S. to other government agencies without a federal court order. This information can be disclosed only if a federal judge determines that, based on the facts submitted in an application authorized by an Assistant Attorney General or his superior, there is reasonable cause to believe that specific criminal act has been committed, that the return or related information is probative evidence of a criminal act, and that the information cannot reasonably be obtained elsewhere. Additionaly, under Section 6103(i)(3), the I.R.S. may (but is not required to) disclose to the agency charged with enforcing federal criminal law any such information that may constitute evidence of a criminal violation.

Under the proposals of S. 732 and S. 1891, however, the I.R.S. would be required to disclose such information given to the I.R.S. by business entities owned by more than two individuals whenever it received a written request from another federal agency. Moreover, if such information "may constitute" evidence of a criminal violation, the I.R.S. on its own initiative must disclose it to other federal agencies (subject, under S. 1891, to some limitations).

IMPACT ON THE BUSINESS COMMUNITY

S. 732 and S. 1891, or legislation containing similar broad disclosure provisions, would pose significant problems for businesses with more than two owners, particularly for smaller firms.

Larger companies are continually under audit by the Internal Revenue Service. The maintain a staff of tax employees who constantly provide I.R.S. personnel with financial and operating data relating to the taxable year or years being audited. However, larger companies do not as a rule forward the information they plan to disclose to the I.R.S. to their corporate counsel's office prior to disclosure. Under S. 732 or S. 1891, businesses necessarily would be hesitant about furnishing information to I.R.S. agents without review by legal counsel familiar with non-tax federal laws that impose criminal sanctions.

The bills would permit a federal agency official having jurisdiction over enforcement of any such laws, who may be considering whether the firm or its customers or suppliers may have violated a criminal statute, to obtain from the I.R.S. on his own written request all of the firm's underlying tax return information, including books and records gathered during the course of an I.R.S. audit. Apparently the I.R.S. agent's supporting memos, analyses and mental impressions would also be subject to disclosure. We need not remind this Subcommittee of the many federal laws that regulate business behavior and impose criminal sanctions. These would include, for example, the Occupational Safety and Health Act, the antitrust laws, the Foreign Corrupt Practices Act, the securities laws, consumer products safety laws and environmental laws. The interpretation and application of these laws are often uncertain.

Proponents of the bill point to the need for more effective means of combatting organized crime, drug trafficking and similar major criminal ventures that confront our society. The Chamber and its many members heartily support a major effort to stamp out these evil forces. But these bils are unnecessarily broad and would authorize disclosure of tax information by the Service to other government agencies seeking to investigate possible violations of a host of business regulatory statutes having no relationship whatever to organized crime, drug trafficking and the like.

For example, S. 1891 would require the I.R.S. to disclose to employees of other agencies on their written request, without court order, information submitted to the I.R.S. by a business with more than two owners in the course of a tax audit if those employees of other agencies are "directly engaged in . . . preparation for any administrative, judicial, or grand jury proceeding (or investigation which may result in such proceeding)" pertaining to "the enforcement of a specifically designated Federal criminal statute (not involving tax administration)." (Proposed new section 6103(i)(2)(A) and (1)(A).)

I respectfully submit that this language is simply too broad and would require the I.R.S. to turn over information to other agencies having jurisdiction over a wide variety of business regulatory laws that have criminal sanctions for violations but have no relationship to organized crime or drug trafficking. I do not wish to indicate that the Department of Justice or other proponents of the bills would intend to use the proposed statute in this fashion, but the possibility of such use should be foreclosed in the statute itself in order that businesses may continue to supply information to the I.R.S. in the course of tax audits without concern that it might be so used.

The possible effect of disclosure to other agencies on their own request would be a matter that would require a company's serious consideration before information is furnished to an examining agent of the I.R.S. Moreover, there would be concern over the possibility of the other agency disclosing the information to potential witnesses, some of whom might be competitors of the taxpayer, as would be permitted by the pending bills.

Smaller firms would be disproportionately affected by S. 732 and S. 1891. When they are audited, they tend to rely on an accountant to prepare, submit and explain the information to the I.R.S. during the course of a tax audit. Lawyers are not customarily involved in tax audits unless and until a tax dispute between the I.R.S. and the taxpayer develops as a result of the audit. Under the pending bills, however, businesses would be hesitant about furnishing confidential information to the I.R.S. without review by a lawyer having knowledge of federal statutes which affect that industry and which contain criminal sanctions. We have a very real concern that this additional burden placed on the already overburdened small business sector would impair the maintenance of a strong and healthy small business community.

S. 732 would make it mandatory for the I.R.S. to disclose information sought by other agencies in two situations. First, the I.R.S. would be required to furnish all underlying return information (other than the return itself) and ancillary documents upon written request of an agency head, the Attorney General or his designee, all without a court order. The section-by-section analysis of the bill states that it is anticipated that the Attorney General would designate the many assistant United States attorneys throughout the country as persons authorized to demand disclosure from the I.R.S. The Attorney General under S. 732 could conceivably designate any Justice Department employee, even one not directly involved in the case. S. 1891 would authorize the written request to be made by a "supervisory-level attorney" in the Department of Justice. While there are advantages to decentralizing the authority to local United States attorneys instead of requiring referral in each instance to Washington, there is strong reason to doubt whether such requests for confidential information should be permitted without court approval and without approval by a United States attorney.

Second, the I.R.S. would be required by S. 732 to disclose on its own initiative such information if it "may constitute" evidence of a violation of a federal criminal law to the agency charged with enforcing the law. I.R.S. agents are not trained to be familiar with the many non-tax federal laws that contain criminal sanctions, nor to analyze information to determine whether it "may" constitute evidence of a violation of any of those laws. Thus neither the agents nor the taxpayer would know during the course of the audit whether the I.R.S. on its own initiative would have to disclose the information to the Department of Justice or other federal agency for consideration under those many non-tax federal laws. We believe such a requirement would impose a most serious burden of decision and review both on the I.R.S. and business taxpayers, and would delay and hamper the administration of the tax laws.

S. 1891 would limit this obligation of the I.R.S. to disclose on its own initiative such information furnished by a corporation or other legal entity by providing that it "may only make such a disclosure if there is reasonable cause to believe such entity was formed or is being operated or maintained with a purpose of facilitating or engaging in Federal criminal activity." (Proposed new section 6103(i)(3)(A).) Once again, however, "Federal criminal activity" can encompass violation of a host of criminal sanctions contained in business regulatory statutes having no relationship to organized crime, drug trafficking and the like. All that would be needed to trigger the requirement would be reasonable cause to believe that a corporation was "being operated or maintained with a purpose [not necessarily the principal purpose] of facilitating or engaging in" violations of some Federal criminal statute, whether a misdemeanor or a felony.

While we appreciate that this language evidences an intention by the draftsmen to limit the application of the provision, we submit that greater restrictions should be imposed. Taxpayers who traditionally have furnished extensive information to I.R.S. agents in the course of tax audits should not be exposed to the possibility that the agent may believe he is required to disclose the information to other government agencies on the ground that it "may" constitute evidence that the corporation has been operated with a purpose of violating some Federal regulatory statute that contains a criminal penalty.

CONCLUSION

The Chamber strongly supports the goal of S. 732 and S. 1891 to provide the nation with greater protection from organized crime. However, we object most seriously to several of the specific provisions of the bills. First, the broad disclosure that would be allowed under the bills would unreasonably burden all businesses and would particularly disadvantage smaller businesses. Second, the disclosure that would be permitted under the bills would be made more onerous by the universe of federal employees able to request information and share it with potential witnesses and others. Third, the I.R.S., through the mandatory disclosure provisions, would be diverted from its primary role of tax administration and enforcement. We respectfully submit that the scope of the bills should be significantly narrowed before one of them is enacted.

Chairman **Rangel**. Well, thank you for your contribution, Mr. Cohen, and I hope that your recommendations would come to us from the Chamber in writing, because of your broad experience, it could be very helpful to us.

Mr. **Cohen**. We have submitted a statement for the record.

We would be pleased to be of such help to you, the committee and your staff as we can.

Chairman **Rangel**. We will be calling on you for some help.

Thank you so much and thank you for waiting.

I think we have one more witness.

Mr. Burch, we will recess for a short while unless you want to submit your statement for the record.

STATEMENT OF MICHAEL S. BURCH, EXECUTIVE DIRECTOR, NATIONAL TAXPAYERS LEGAL FUND

Mr. **Burch**. I will just do that.

Chairman **Rangel**. OK; Mr. Michael Burch, the executive director of the National Taxpayers Legal Fund, your full statement will appear in the record and the committee will be reaching out to you for some questions.

[The prepared statement follows:]

STATEMENT OF MICHAEL S. BURCH, EXECUTIVE DIRECTOR, THE NATIONAL TAXPAYERS LEGAL FUND

I want to thank you Mr. Chairman, for the opportunity to testify this morning. My name is Michael Burch and I am the Executive Director of the National Taxpayers Legal Fund, a grassroots taxpayers advocacy group with over 13,000 members nationwide. Our chairman is former Senator Eugene J. McCarthy and our organization, as it represents the views of the average taxpayer, is very much concerned with privacy issues. Because of that concern, we are extremely apprehensive about any changes in the 1976 Tax Reform Act that makes tax returns and related information more readily available to agencies other than the Internal Revenue Service.

It is important to remember the genesis of the Tax Reform Act, to understand both its importance and why proposals to weaken the act, however well intentioned they may be, are fundamentally misguided. The Tax Reform Act was not created ex nihil. It did not come about because members of Congress had some idle time on their hands and thought to close up a possible hole in the nation's tax law. The Tax Reform Act resulted from months of congressional testimony and investigation into abuses against individual taxpayers at the federal and state levels that had occurred over a period of years. The Tax Reform Act was not a hastily conceived piece of legislation either. It was carefully crafted to balance the needs of the I.R.S. as well as to protect the rights and liberties of the American taxpayer.

It is obvious, looking at the act, that those who drafted it were aware of the importance of the issues involved. The question of taxpayer privacy is a massive and important one affecting the most fundamental rights we enjoy as citizens of this country. It is equally important from a pragmatic viewpoint as well. Taxpayers and their incomes are largely responsible for supplying the money on which this country runs, and if through carelessness we endanger their voluntary payment of taxes, then the country itself is threatened.

If it is granted that the issue of taxpayer privacy is important, then it should follow that only under the strongest compulson and for very good reasons, should the laws protecting taxpayers privacy be lessened. Mr. Chairman and members of this committee, I respectfully submit to you that the case against weakening the tax legislation is very strong indeed, and that the arguments for it are, at best, unconvincing.

The most obvious argument against making taxpayer information more readily available to other levels and branches of government as a non-tax law enforcement tool, is both the uniqueness of the information involved and the role of the I.R.S. in obtaining it. The I.R.S. is, as its name suggests, an agency designed to collect tax revenues and administer and enforce tax laws. It was not created to trap drug pushers, apprehend murders, or foil bank robbers. There are other agencies of the government whose job are to perform these tasks. The I.R.S. is a tax collecting agency, period. The I.R.S. has testified numerous times in the past that it is unable to keep pace with the avalanche of work poured upon it because of time, budgetary and personnel considerations. And now proponents of new legislation come along asking the already beleagured agency to take on even more work. This is also irrespective of the fact that the I.R.S. itself has repeatedly testified that it disagrees with such legislation.

There is also an insidious aspect to these proposals that has been uncommented upon, I believe, and that is the blurring of lines between governmental agencies. It is fitting and practical that Governmental agencies are separated. Although duplication of effort is often a probable result, it makes these agencies more managable and most importantly, more easy to oversee. It has the same effects that separation of powers has on the federal government. The tendency evident in this legislation is to move disparate but powerful agencies together. We have already seen the abuses that resulted when other agencies have had access to I.R.S. records, and legislative proposals that would serve to link these agencies together again represent a very real treat, not just to the privacy of individuals, but to our entire system of government. The prospect of one super-agency with vast discretionary powers over the lives of all Americans is a terrifying prospect to contemplate. For this, if for no other reason, we should think most carefully about legislative attempts to bind agencies together.

The most obvious argument against such legislation, of course, is that it is superfluous as there is already a section of the Internal Revenue Code, 6103(i), that allows other agencies of the government to obtain sensitive taxpayer information. It is our belief that this section is more than adequate tool for law enforcement.

Those who propose scraping this section must prove that the law as it stands constitutes a major roadblock to their operations before even thinking about changing such laws as we currently have. We believe that not only can such a case not be made but that there is real cause to believe that the people pushing for such changes are not even utilizing the advantages of Section 6103.

I would refer you to the printed record of earlier hearings on this same issue held before this committee on July 30, 1980. As part of the material submitted to this committee by then Deputy Assistant Attorney General Irvin B. Nathan was a summary of a questionnaire sent out by the Department of Justice to all federal prosecutors in late 1979 after Section 6103(i) had been in effect some three years. The responses to the questionnaire were interesting, but most interesting of all was the section that dealt with the Department's use of section 6103. I refer you to page 81 of those hearings, the last paragraph of which reads as follows: "Finally, one office stated that most Assistant United States Attorneys are unfamiliar with Section 6103 and its procedures, and therefore usually do not make use of the statute to obtain tax information. This office stated that the Department of Justice can and should take steps to educate Government attorneys regarding Section 6103, either through the Attorney General's Advocacy Institute or through a separate seminar."

Again in December 1979 Peter Bensingen, the Administrator of the Drug Enforcement Agency, testified before the Senate Permanent Subcommittee on Investigations, that D.E.A. records showed never having received any disclosures from I.R.S. even though his agency could solicit information from them. What the evidence suggests is not that it is too difficult to obtain information but rather that no one is utilizing the law effectively as it currently stands.

This leads me to another point in connection with Section 6103 that stands in direct opposition to proposals to mitigate it. We believe that far from it being difficult to obtain tax information under Section 6103 that it is, in fact, far too easy. The key here is the language that allows I.R.S. to release such information on "reasonable" cause. This language is the flimsiest of restrictions and violates our traditional granting of ex parte orders on probable cause based on solid evidence. Section 6103 obviates the need for direct evidence or probable cause. We respectfully suggest that if Section 6103 is to be changed, then it should be tightened.

To conclude we would remind you again, Mr. Chairman, of the enormity of the issues involved here. We have all witnessed laws and actions by the Government that have initially been described by their proponents as good, only to discover too late, that they were, in fact, pernicious. Section 6103 was erected because it grew out of laws that seemed good but were abused. Now you are being asked to reverse that change. Mr. Chairman, this is a deliberative body and it is important that you carefully examine this legislation and any proposed changes. You must ask hard questions. Questions like: What reason is there to believe that once this information is made more readily available, that taxpayers won't be abused again? Why haven't the departments of government that want the law changed educated their own people about the current law? And finally, is this legislation worth the further deterioration of the relationship between the people of this country and their government.

Taxpayer data as it now stands constitutes a virtual violation of the average citizen's Fourth and Fifth amendment rights. Given the coercive nature of taxation and the growing resentment between taxpayers and the I.R.S., we should think most carefully about legislation that allows people to be abused. Every scrap of testimony made by the I.R.S. that I've seen stated that there was a direct relationship between the amount of money collected and the confidentially of information obtained. There is little question that legislation that disseminates such tax information is not merely wrong but has the potential to undermine the very nature of our taxing system.

Chairman **Rangel**. The committee stands adjourned, subject to the call of the Chair.

[Whereupon, at 5:30 p.m., the hearing was adjourned.]

[The following were submitted for the record:]

STATEMENT OF HON. WILLIAM V. ROTH, JR., A U.S. SENATOR FROM THE STATE OF DELAWARE

During recent weeks, the Senate Permanent Subcommittee on Investigations, under my Chairmanship, has once again heard compelling testimony concerning the need to amend our tax laws to insure that major criminal offenders are not the beneficiaries of tax law provisions otherwise properly conceived to protect taxpayers in general.

In Subcommittee hearings during October and November of this year, we have clearly seen how the current tax laws continue to frustrate the effective enforcement of Federal criminal statutes aimed at organized crime and narcotics trafficking. This testimony is similar to that heard in prior Subcommittee hearings. Members of the Permanent Subcommittee on Investigations have led the effort in the past to correct these shortcomings.

Under the able direction of our ranking minority member, Sam Nunn, a set of amendments passed the Senate earlier this year as part of the Economic Recovery Tax Act of 1981 but were not agreed to in conference although the conferees agreed that congressional attention in this area was warranted. I have supported Senator Nunn in his efforts and have cosponsored his proposed legislation in this area, S. 732.

Due in large part, I believe, to the past work of Senator Nunn and the recent efforts of the Subcommittee, the administration has finally responded with its own legislative recommendations on this matter. The administration's proposals have marked similarities with S. 732 and are in general accord with the objectives to be sought. The differences between the administration proposal and S. 732 are, in my opinion, matters which can be quickly and effectively resolved. To insure an expeditious resolution between these proposals, I have considered it appropriate for me, as Chairman of the Permanent Subcommittee on Investigations, and one who is vitally interested in developing and refining federal responses to crime in America, to introduce S. 1891, the "Tax Disclosure and Summons Amendments" to Title 26. This bill has the enthusiastic support of many law enforcement officials.

Both Senator Nunn and I are working towards an early consideration of these bills before the Senate Finance Committee. We support the effort of the Ways and Means Committee in these hearings to consider the important issues surrounding amendments to Section 6103 of the Internal Revenue Code. I would emphasize that, while I, like many of you, have always been greatly concerned over the maintenance of individual privacy rights, I believe that the Senate bills introduced by Senator Nunn and myself maintain the necessary and essential balance between those rights and the significant needs of our law enforcement agencies which, unfortunately, seem to be losing the ongoing war against the major criminal elements in our society particularly in the areas of organized crime and narcotics trafficking.

I would gladly extend to your Committee any staff assistance that our Subcommittee might offer as you proceed in your careful review of the issues at hand.

Statement of Hon. Warren Rudman, a U.S. Senator From the State of New Hampshire

As Vice Chairman of the Senate Permanent Subcommittee on Investigations, I have become well acquainted with the issue faced by the Subcommittee on Oversight today. Evidence developed before the Permanent Subcommittee on Investigations over the course of several hearings has indicated that the good intentions surrounding the enactment of the so-called Tax Reform Act of 1976 have resulted in serious problems for Department of Justice and Department of Treasury personnel who are attempting to enforce the criminal laws of the United States. During the course of extensive hearings held before the Subcommittee in November on international narcotics trafficking, we heard testimony from prosecutors and traffickers alike which indicated that the attempted reforms enacted in 1976 have created a stone wall between IRS agents and prosecutors which can only be described as a tragic development.

For example, during our recent hearings a prosecutor was asked what caused his reluctance to use IRS agents in complex narcotics investigations. He replied, "to a man, they are very capable, competent and are restricted by their regulations and requirements to an extent that they are not of any help to us and are in fact, a hindrance." The prosecutor went on to say that these restrictions make it "impossible for [IRS agents] to be productive members of a team to investigate and prosecute a case." When asked whether the Tax Reform Act of 1976 and the regulations that have issued therefrom were the basis of the problem, the prosecutor replied, "Yes, those have caused them to be ineffective in this area of investigation." When asked to comment on the attitude of IRS agents about these restrictions, he testified, "individually, it is frustration to the point of almost giving up the fight."

This is the type of testimony which the Permanent Subcommittee on Investigations has heard over and over again. The oppportunity to make substantial improvements in this situation is at hand and I would urge this Subcommittee to seriously consider the type of measures which have been proposed in the Senate in S. 732 introduced by Senator Nunn and cosponsored by me, and also in S. 1891 introduced by Senator Roth, a measure I have also co-sponsored.

Thank you for this opportunity to present my views.

STATE OF MAINE,
DEPARTMENT OF FINANCE AND ADMINISTRATION,
Augusta, Maine, January 27, 1982.

Re hearings on taxpayer privacy issues.

Hon. CHARLES B. RANGEL,
Chairman, House Ways and Means Oversight Subcommittee,
Longworth House Building, Washington, D.C.

DEAR CONGRESSMAN RANGEL: The issues addressed in the Oversight Subcommittee hearing on the review of Section 6103(i) of the Internal Revenue Code and bills to amend this section are relevant to the State of Maine and the administration of Maine's taxes.

I would recommend:

1. the Code be amended to provide that Section 6103(i) be the only provision under which federal authorities could seek state tax returns or return information;
2. the state tax administrator, on whom the subpoena would be served, would be a party to the hearing before a judge, with equal standing with the federal official seeking the subpoena;
3. the present standards in Section 6102(i) should not be amended with respect to the subpoena of state tax returns and/or information;
4. a state tax official who produces state tax returns pursuant to a federal court order issued under Section 6103(i) should not be liable to criminal or civil sanction provided in any applicable state confidentiality law.

Your serious consideration of my recommendations will be sincerely appreciated.

Sincerely,

RODNEY L. SCRIBNER,
Commissioner.

MINEOLA, N.Y., *January 29, 1982.*

Hon. CHARLES B. RANGEL,
Chairman, House Ways and Means Oversight Committee,
Longworth House Office Building, Washington, D.C.

HONORABLE SIR: On behalf of the Federal Law Enforcement Officers' Association (FLEOA), an organization composed of nearly 7,000 professional Law Enforcement Officers working for the Federal Government, we would like to express our views with regard to the privacy provisions covering information submitted by taxpayers as part of their Federal tax returns.

As you are aware, in its revision of the Tax Code undertaken in 1976, Congress enacted a privacy provision protecting tax returns and information contained therein from disclosure except under certain specified conditions. That provision is now codified as 26 U.S.C. 6103(i).

FLEOA requests that Congress, in evaluating the effect of this law, not disregard the law enforcement effects that it has. We note with approval, for instance, that the law has been amended to exclude the name and address of a taxpayer from the protected category of return information. More centrally, FLEOA calls your attention to the fact that the abuses which this law was proposed to correct were political in origin, and were not law enforcement abuses. Even under the prior law, tax returns were used by law enforcement agencies in a careful and controlled fashion. See, for instance, the statistics set forth in Senate Report 94-938 at 326 et seq.

The need for access to tax payer information as part of bona fide and fully Constitutional law enforcement procedure has been fully stated in hearings held even before the tax Reform Act of 1976. We call to your attention the examples set forth in the Hearings before the Senate Subcommittee on Administration of the Internal Revenue Code, Committee on Finance, April 21, 1975 at 75-80. We fully agree with Senator Weicker's desire that the Internal Revenue Commission not be a "lending Library" id. at 201. However, since the time of those hearings, we have seen the advent of more and more sophisticated forms of white collar crime, and the development of almost unlimited money laundering capabilities engendered by the burgeoning traffic in illegal drugs. This places the need for access to taxpayer information, obtained under proper safeguards, into high relief. In this connection, we propose that section 6103(i)(B)(ii) might well be amended to permit access if reasonable cause can be shown that taxpayer information would lead to probative evidence of crime, even if the information itself does not constitute such evidence. Likewise, while we agree that a non-articulable suspicion of crime should not trigger access to taxpayer information, section 6103(i)(B)(i) should be amended to make clear that where there exists reasonable cause to believe that a crime has been committed, the investigator should not be required to show (without the very evidence which is determinative) which specific statute has been violated. We suggest that a showing of reasonable belief that an act has been committed which, if committed, would be a violation of law, is sufficient. The statute, as it stands, admits of such a reading. We suggest that it be clarified.

We repeat, political or personal access to taxpayer information was the evil which this section was aimed at. In curing that evil, and overseeing the cure, we urge Congress not to hinder legitimate law enforcement efforts, which use taxpayer information to detect crimes.

Thank you for this opportunity to make our concerns heard.

Respectfully submitted,

JACK B. SOLERWITZ,
By DAVID S. HELLER,
On Behalf of Federal Law Enforcement Officers' Association.

OFFICES OF THE ATTORNEY GENERAL,
Baltimore, Md., February 18, 1982.

CHARLES B. RANGEL,
Rayburn Building,
Washington, D.C. 20515

DEAR CONGRESSMAN RANGEL: The National Association of Attorneys General (NAAG) has advised me that you seek certain information concerning the need for changes in the disclosure provisions of the Tax Reform Act of 1976. I wish to respond to your questions as posed by NAAG.

1. Has the Tax Reform Act of 1976 hampered any state investigations, and if so, how?

The disclosure provisions of the Tax Reform Act hamper any State white-collar crime investigation unless enforcement of the State's tax laws is part of the investigative effort. Under 26 U.S.C. 6103(d), federal income tax return information can only be disclosed to State agencies for the purpose of "tax administration"; thus, only the tax investigator-prosecutor may obtain federal return information which often contains critical leads to a target's financial dealings.

2. If disclosure to state Attorneys General were permitted, what types of cases would the disclosure of such information help you bring?

Such disclosure would be of invaluable assistance to our prosecutions of white-collar crime, public corruption, medicaid fraud, and violations of Maryland's anti-trust, securities, and hazardous waste laws.

3. Can you describe a case where no other evidence existed but where you feel you would be able to obtain a conviction if disclosure of information in possession of the IRS were permitted? The Subcommittee has asked for examples that occur with regularity, rather than isolated incidents.

Our investigations of the above-listed crimes regularly encounter stumbling blocks in fleshing out our picture of a target's financial dealings. Federal returns should provide sufficient detail to identify the flow of funds to the taxpayer as income and the flow from him as business-related expenses. Maryland returns, by law, adopt federal tax figures without detail; thus, lacking federal return information, the figures on the State return are virtually meaningless.

4. If a provision to allow disclosure specifically to state Attorneys General were enacted, would you object if you were held criminally and/or personally liable for redisclosure?

We would not oppose the imposition of criminal sanctions for willful violations of disclosure provisions.

5. Is this type of information currently available through your state taxing authority?

Under Maryland law, the limited information contained in a State tax return is obtainable for investigative purposes by court order.

6. Have you had any experience under 26 U.S.C. 6103 and, if so, could you comment on that experience?

Our experience with disclosure for purposes of "tax administration" under 26 U.S.C. 6103 has been that information is produced by the IRS at a snail's pace.

I hope that these comments will be of assistance to you and the Oversight Subcommittee.

Sincerely,

Stephen H. Sachs,
Attorney General.

The State of Nevada,
Executive Chamber,
Carson City, Nev., February 5, 1982.

Hon. Charles B. Rangel,
Chairman, Subcommittee on Oversight,
Committee on Ways and Means,
Washington, D.C.

Dear Congressman Rangel: I am informed that your subcommittee is currently considering amendment to Section 6103(i) of the Internal Revenue Code as contained in H.R. 1502, S. 732 and S. 1891. Testimony on these amendments has included that of Mr. Owen L. Clark, Deputy Commissioner, Multistate, Massachusetts Department of Revenue.

Like Massachusetts, Nevada is concerned over the release of confidential state tax information in connection with nontax criminal investigations through the use of a federal subpoena or an ex parte court order. While I certainly support the utilization of any pertinent information in the prosecution of serious crimes, I believe that some parameters for release of state tax information must be established to protect the integrity of state confidentiality statutes and the rights of taxpayers.

Accordingly, I support the Massachusetts proposal that amendments to Section 6103(i) include:

1. A separate subsection relating to state tax administration and to the use of state tax returns by federal officials in a non-tax criminal proceeding.
2. That Section 6103(i) be the only and exclusive provision under which state tax returns, information on such returns or third party information can be subpoenaed.
3. That the state tax administrator whose returns or information gleaned from such returns is sought by federal subpoena shall be a party to any hearing with equal standing with the federal official seeking the issuance of the subpoena.
4. The present standards in Section 6103(i)(1) shall not be amended when state tax returns or information is sought.
5. Any state tax official who, pursuant to a court order issued under Section 6103(i), produces such returns or information, or who is compelled to testify before a federal agency or court shall not be liable for any criminal or civil sanction even if the law of that state prohibits the disclosure of tax returns or the information contained in such returns.

Your assistance in insuring that these amendments are incorporated in the Internal Revenue Code would be appreciated.

Sincerely,

Robert List, *Governor.*

APPENDIX

COMPARISON OF PROPOSALS RELATING TO THE DISCLOSURE OF TAX INFORMATION FOR PURPOSES OF NONTAX CRIMINAL LAW ENFORCEMENT

H.R. 1502, introduced by Mr. Gibbons (similar to S. 732, introduced by Senators Nunn, Chiles, *et*. *al*.) and S. 1891, introduced by Senators Roth, Nunn, *et*. *al*. (the Administration's proposal).

SCHEDULED FOR A HEARING BY THE WAYS AND MEANS SUBCOMMITTEE ON OVERSIGHT
ON DECEMBER 14, 1981

PREPARED BY THE STAFF OF THE JOINT COMMITTEE ON TAXATION
DECEMBER 10, 1981

JCX-39-81

INTRODUCTION

The Oversight Subcommittee of the Committee on Ways and Means has scheduled a public hearing on December 14, 1981, on the subject of disclosure of tax returns and return information in connection with nontax criminal law enforcement and other taxpayer privacy issues.

In announcing the hearing, the Subcommittee indicated that it intends to examine the following areas relating to disclosure of tax returns and return information (Subcommittee Press Release #12, dated December 3, 1981):

"(a) The extent to which I.R.C. Section 6103 (i) has served to protect taxpayers from unwarranted governmental intrusion resulting from their compliance with the tax laws.

(b) Whether I.R.C. Section 6103 (i) has provided an appropriate balance between taxpayers' rights to privacy and the law enforcement agencies' investigative needs.

(c) The Administrations's efforts to coordinate and to operate fully and efficiently within the parameters of the law.

(d) How various proposed changes to existing law would affect current disclosure practices, taxpayer compliance, and law enforcement efforts."

This document, prepared in connection with the Subcommittee hearing, provides a comparison of the provisions of present law and two proposals (H. R. 1502, Mr. Gibbons, and S. 1891, the Administration proposal) relating to disclosure of tax information for purposes of nontax criminal law enforcement.

Present Law	H.R. 1502	S. 1891
Categories of Tax Information For purposes of disclosure, present law divides tax information into three broad categories: (1) returns, (2) return information, and (3) taxpayer return information. A return is any tax or information return, declaration of estimated tax, or claim for refund which is required (or permitted) to be filed by, or on behalf of, or with respect to, any person. (A return also is any amendment, supplemental schedule, or attachment filed with the tax return, information return, etc.) Return information is certain data relating to a particular taxpayer, including the following items: the taxpayer's identity and the nature, source, or amount of his income, payments, receipts, deductions, exemptions, credits, assets, liabilities, net worth, tax liability, tax withheld, deficiencies, overassessments, and tax payments. Taxpayer return information is return information that is filed with, or furnished to, the IRS by, or on behalf of, the taxpayer to whom the return relates. (This includes, for example, data supplied by a taxpayer's representative to the IRS in connection with an audit.)	Categories of Tax Information For purposes of disclosure, the bill would divide tax information into two categories: (1) return information and (2) nonreturn information. Return information would be a tax return, information return, declaration of estimated tax, or claim for refund, as well as any amendment or supplement thereto, that is filed by, on behalf of, or with respect to, any person (*i.e.* return information generally would mean the same as returns under present law). Return information also would be any information provided to the Secretary by, or on behalf of, an individual taxpayer to whom the information relates. For this purpose, an individual taxpayer would be any natural person or a corporation, partnership, association, union, or other entity consisting of no more than two owners, shareholders, partners, or members. Nonreturn information generally would be any information (other than a return) that is provided to the Secretary by, or on behalf of, someone other than the taxpayer to whom the information relates (*e.g.*, information with respect to an individual that is submitted by a third-party). In addition, nonreturn information would include any information (other than a return) that relates to any corporation, partnership, association, union, or other entity consisting of more than two owners, shareholders, partners, or members.	Categories of Tax Information For purposes of disclosure, the bill would divide tax information into two categories: (1) investigative return information and (2) investigative nonreturn information. Investigative return information generally would have the same meaning as return information under H.R. 1502 (*i.e.*, it would include returns of all taxpayers and underlying records and information submitted by, or on behalf of, individual taxpayers). An individual taxpayer would be a natural person or a corporation, partnership, association, trust, estate, or other entity consisting of no more than two individual owners, shareholders, partners, members, or trustees. Investigative nonreturn information generally would have the same meaning as nonreturn information under H.R. 1502 (*i.e.*, primarily the underlying books and records submitted to the IRS by, or on behalf of, larger corporations and information received from third parties during IRS investigations).

Present Law	H.R. 1502	S. 1891
Disclosure Pursuant to Court Order Returns and taxpayer return information may be disclosed by the IRS to other Federal agencies, for purposes of nontax criminal investigations, only upon the grant of an *ex parte* order by a Federal district court judge.	**Disclosure Pursuant to Court Order** Return information would be available from the IRS only pursuant to the order of a Federal district court judge or magistrate. Such order could provide for continuous disclosure.	**Disclosure Pursuant to Court Order** Investigative return information would be available from the IRS only pursuant to the order of a United States district court judge or magistrate. Such order could provide for continuous disclosure.
Individuals Permitted to Apply for Court Order The head of a Federal agency or, in the case of the Department of Justice, the Attorney General, the Deputy Attorney General, or an Assistant Attorney General may authorize an application to a Federal district court judge for the disclosure of returns or taxpayer return information.	**Individuals Permitted to Apply for Court Order** The Attorney General, the Deputy Attorney General, an Assistant Attorney General, a United States Attorney, or the attorney in charge of a criminal division organized crime strike force could authorize the disclosure application.	**Individuals Permitted to Apply for Court Order** Similar to H.R. 1502, except that the Associate Attorney General also could authorize the disclosure application.
Standards for Granting of Court Order An *ex parte* order may be granted upon the determination of the judge that: (1) there is reasonable cause to believe, based upon information believed to be reliable, that a specific criminal act has been committed; (2) there is reason to believe that the return or return information is probative evidence of a matter in issue related to the commission of the criminal act; and (3) the information sought to be disclosed cannot reasonably be obtained from any other source, unless the information is the most probative evidence of a matter in issue relating to the commission of the criminal act.	**Standards for Granting of Court Order** An *ex parte* order would be granted upon a showing that: (1) there is reasonable cause to believe, based upon information believed to be reliable, that a specific criminal act has been, or is being, committed; (2) the information is being sought exclusively for use in a Federal criminal investigation or proceeding concerning such criminal act; and (3) there is reasonable cause to believe that the information may be relevant to a matter relating to the commission of such criminal act.	**Standards for Granting of Court Order** The standards for issuing an *ex parte* order are similar to those contained in H.R. 1502. In addition, an *ex parte* order also could be granted upon a determination that: (1) an arrest warrant has been issued for an individual who is a fugitive from justice; (2) the information is sought exclusively for use in locating such individual; and (3) there is reasonable cause to believe that the information may be relevant to determining the location of the individual.

Present Law	H.R. 1502	S. 1891
Disclosure Pursuant to Written Request Return information, other than taxpayer return information, may be disclosed upon written request from the head of a Federal agency, the Attorney General, Deputy Attorney General, or an Assistant Attorney General. This written request must set forth: (1) the name and address of the taxpayer with respect to whom the information relates; (2) the taxable period or periods involved; (3) the statutory authority under which the proceeding or investigation (to which the information is relative) is being conducted; and (4) the specific reason or reasons why the disclosure is or may be material to the proceeding or investigation.	Disclosure Pursuant to Written Request Nonreturn information could be disclosed upon written request from the head of a Federal agency, an Inspector General, or the Attorney General or his designee. This written request would be required to set forth: (1) the name and address of the taxpayer with respect to whom the information relates; (2) the taxable period or periods involved; (3) the statutory authority under which the proceeding or investigation (to which the information is relative) is being conducted; and (4) allegations of criminal conduct giving rise to the proceeding or investigation. Nonreturn information could be redisclosed to other Federal Government personnel or witnesses deemed necessary for assistance during the criminal investigation or in preparation for an administrative, judicial, or grand jury proceeding. For purposes of this provision, the name, address, and social security number of the taxpayer, whether a taxpayer filed a return for a given year or years, and whether there is or has been a criminal investigation of a taxpayer would be treated as nonreturn information.	Disclosure Pursuant to Written Request Investigative nonreturn information could be disclosed upon written request from the head of a Federal agency, an Inspector General, the Attorney General, the Deputy Attorney General, the Associate Attorney General, an Assistant Attorney General, the attorney in charge of a criminal division organized crime strike force, or a supervisory-level attorney for the Government designated by the Attorney General. The written request for disclosure would be required to set forth the same information specified in H.R. 1502. Investigative nonreturn information could be redisclosed to other Federal Government personnel or potential witnesses.
Disclosure of Tax Information Concerning Possible Criminal Activities The IRS is authorized (but not required) to disclose return information, other than taxpayer return information, that may constitute evidence of a violation of Federal criminal laws to the extent necessary to apprise the head of the appropriate Federal agency charged with the responsibility of enforcing those laws.	Disclosure of Tax Information Concerning Possible Criminal Activities The bill would require the IRS to disclose, as soon as practicable, any nonreturn information that may constitute evidence of a violation of Federal criminal laws. Furthermore, if the IRS makes a recommendation to the Department of Justice for prosecution for a violation of the Internal Revenue Code, any return or nonreturn information reviewed, developed, or obtained during the tax investigation that may constitute evidence of a violation of Federal criminal laws would be	Disclosure of Tax Information Concerning Possible Criminal Activities Generally, similar to H.R. 1502. However, to the extent that a disclosure would be based upon information furnished by, or on behalf of, a corporation partnership, association trust, estate, or other legal entity, IRS-initiated disclosure would be permitted only if there was reasonable cause to believe such entity was formed, or is being operated or maintained, with a purpose

EDITED FROM

Congressional Research Service
The Library of Congress

Washington, D.C. 20540

DOCUMENT PREPARED
FOR THE
WAYS AND MEANS OVERSIGHT SUBCOMMITTEE

TAX RETURN CONFIDENTIALITY: A SUMMARY OF THE EXISTING LAW AND ITS RECENT RECONSIDERATION

by
Howard M. Zaritsky
Legislative Attorney
American Law Division
October 20, 1981

and

Thomas B. Ripy
Legislative Attorney
American Law Division
December 3, 1981

TABLE OF CONTENTS

I. Background: A History of the Events Leading to the 1976 Tax Reform Act Rules on Tax Return Confidentiality SC-1

II. Principal Areas of Revision in the Tax Reform Act of 1976 . . . . SC-4

III. Analysis of S.732 and H.R. 1502 (97th Cong.). . SC-7

IV. Justifications for and Questions Raised by Proposed Changes SC-7

TAX RETURN CONFIDENTIALITY: A SUMMARY OF THE EXISTING LAW AND ITS RECENT RECONSIDERATION

Federal tax returns are confidential records disclosed by the Internal Revenue Service and other governmental agencies only in specific statutorily delineated situations. Until 1976, however, tax returns were public documents open to disclosure under not only statutory guidelines, but also extensive regulations and Executive Orders. This report summarizes the developments leading to the revision of the rules on tax return confidentiality in 1976, and the main areas in which the law was revised. It also provides a chronology of the developments in the revision of the tax return confidentiality rules and recent reconsideration of this subject.

I. BACKGROUND: A HISTORY OF THE EVENTS LEADING TO THE 1976 TAX REFORM ACT RULES ON TAX RETURN CONFIDENTIALITY.

The history of tax return confidentiality may be traced to the Civil War Income Tax Act of 1862[1/], when tax information was posted on court house doors and sometimes published in newspapers to promote taxpayer surveillance of neighbors, but the events directly leading to the revision of these laws in 1976 are directly traced to Executive Orders 11697 and 11709, issued by former President Richard M. Nixon authorizing the Department of Agriculture to inspect the tax returns of all farmers "for statistical purposes."

Executive Order 11697 was issued on January 17, 1973, opening the income

---

[1/] Act of July 1, 1862, ch. 119, 12 Stat. 473; see generally on the history of tax return confidentiality, Whitaker, "Taxpayer Privacy vs. Freedom of Information: Proposals to Amend Sec. 6103," 6 Tax Adviser 198 (1975); and Zaritsky, "Legislative History of Tax Return Confidentiality: Section 6103 of the Internal Revenue Code of 1954 and Its Predecessors," CRS Report 74-211A (December 4, 1974).

tax returns of all farmers to inspection by the Department of Agriculture.[2] On March 27, 1973, Executive Order 11709 limited the scope of the earlier order consistent with Treasury regulations on disclosure.[3]

During 1973, two subcommittees of the House of Representatives held hearings regarding the Department of Agriculture's need for the tax data disclosed by the two executive orders.[4] During these hearings, sentiments against the orders were expressed. Officers of the Department of Justice testified that the two orders were prototypes for future orders opening other tax returns to inspection by other agencies. Responding to the adverse sentiment expressed in these two hearings, the President revoked both orders on March 21, 1974.

The concern over tax return confidentiality that remained after revocation of the two orders was increased by disclosures made in hearings of both the Senate Select Committee on Presidential Campaign Activities (Watergate Committee)[5] and the House Judiciary Committee investigating the possible

---

[2] Ex. Order 11697, 38 Fed. Register 2332 (January 24, 1973).

[3] Ex. Order 11709, 38 Fed. Register 8131 (March 29, 1973).

[4] Hearings before the Subcommittee on Department Operations of the Committee on Agriculture, House of Representatives, "Inspection of Farmers' Federal Income Tax Returns by the U.S. Department of Agriculture," 93d Cong., 1st Sess. (1973); and Hearings before a Subcommittee of the Committee on Government Operations, House of Representatives, "Executive Orders 11697 and 11709 Permitting Inspection by the Department of Agricuture of Farmers' Income Tax Returns," 93d Cong., 1st Sess. (1973).

[5] Hearings beore the Select Committee on Presidential Campaign Activities, United States Senate, 93d Cong., 2d Sess. part 1 (1974).

Impeachment of President Nixon.[6] The Watergate Committee's hearings revealed that former White House counsel John Dean had sought from the I.R.S. political information on so-called "enemies." Furthermore, it was disclosed to that committee that the White House actually was supplied information on I.R.S. investigations of Howard Hughes and Charles Rebozo. The committee noted that tax information and income tax audits were commonly requested by White House staff and supplied by other IRS personnel.[7]

The House Judiciary Committee's impeachment inquiry also revealed apparently unauthorized use of I.R.S. tax data by the President. One of the Articles of Impeachment proposed by the Judiciary Committee alleged that President Nixon had:

> endeavored to obtain from the Internal Revenue Service, in violation of the constitutional rights of citizens, confidential information contained in income tax returns for purposes not authorized by law. . . .[8]

Congressional interest in tax return confidentiality also manifested itself in 1974 when, as part of the Privacy Act of 1974,[9] Congress ordered the newly-established Privacy Protection Study Commission to report to the President and Congress on the proper restrictions which should be placed on the disclosure of Federal income tax information. This report was issued on June 9, 1976, and suggested major changes in the distribution of tax data to the Department of Justice for both tax and non-tax law enforcement, distribution of tax data to the states and to local governments, and transfer of information to the President and the executive agencies. It also recommended more severe penalties for wrongful disclosure of tax data. The commission did not recommend a general denial of tax data to non-tax Federal agencies.[10]

---

[6] Hearings before the Committee on the Judiciary, House of Representatives, "Pursuant to H.Res. 803, A Resolution Authorizing and Directing the Committee on the Judiciary to Investigate whether Sufficient Grounds Exist for the House of Representatives to Exercise its Constitutional Power to Impeach Richard M. Nixon, President of the United States of America," 93d Cong., 2d Sess. book VIII (1974).

[7] S. Rep. No. 981, 94th Cong., 2d Sess. 130-142 (1974).

[8] H. Rep. No. 1305, 94th Cong., 2d Sess. 3, 141-145 (1974).

[9] Pub. L. 93-579 § 5(c)(2)(B)(ii), 93d Cong., 2d Sess. (1974).

On June 10, 1976, the Senate Finance Committee issued its report on H.R. 10612, the Tax Reform Act of 1976, in which it proposed substantial revisions in the rules governing tax return confidentiality.[11] The Finance Committee's proposal dealt with the same general issues as had the Privacy Protection Study Commission's report, but it resolved them differently. With few technical changes, the Conference Committee on H.R. 10612 adopted the Senate Finance Committee's version of the tax confidentiality rules[12] as part of the Tax Reform Act of 1976 (1976 Act).[13]

II. PRINCIPAL AREAS OF REVISION IN THE TAX REFORM ACT OF 1976.

The Tax Reform Act of 1976 entirely revised the rules on tax return confidentiality. The six areas that received the greatest consideration in 1976 included (1) disclosure of tax data to the Justice Department for use in civil and criminal tax matters, (2) *disclosure of tax data for use in criminal non-tax matters,* (3) disclosure of tax data for use in civil non-tax matters, (4) disclosure of tax data to the Executive Office of the President, (5) disclosure of tax data to the Congress and its committees, and (6) disclosure of tax data to State and local governments.

---

[10] "Federal Tax Return Confidentiality," Report of the Privacy Protection Study Commission (June 1976).

[11] S. Rep. No. 938, 94th Cong., 2d Sess., Part I, 315-348 (1976).

[12] S. Rep. No. 1236, 94th Cong., 2d Sess. 475-483 (1976).

[13] Pub. L. 94-455 § 1202, 94th Cong., 2d Sess. (1976).

B. *Disclosure of Tax Data for Use in Criminal Non-Tax Matters.* Prior to the 1976 Act, Treasury Regulations permitted disclosure of tax information to attorneys in the Department of Justice in any non-tax criminal matter in which the information was deemed "necessary in the performance of" the attorney's "official duties."[22] A written statement signed by the Attorney General, Deputy Attorney General, an Assistant Attorney General, or a U.S. Attorney was required, identifying the taxpayer, the tax involved, the taxable period, and the reason for the request.

The 1976 Act provides that tax return information and returns received from or on behalf of a taxpayer are not disclosed to the Department of Justice for use in non-tax criminal matters unless the Department of Justice first obtains an *ex parte* order from a Federal district judge to the effect that there is reasonable ground to believe that a specific criminal act has been committed, there is reason to believe that the return or return information is probative evidence in respect of that criminal act, and that the information sought cannot be reasonably obtained from any other source. The Treasury Secretary can still refuse to provide the information if he or she determines

---

[22] Former Treas. Regs. § 301.6103(a)-1(g).

Present Law	H.R. 1502	S. 1891
Disclosure of Tax Information Concerning Possible Criminal Activities (cont'd.)	Disclosure of Tax Information Concerning Possible Criminal Activities (cont'd.) required to be furnished to the Department of Justice.	Disclosure of Tax Information Concerning Possible Criminal Activities (cont'd.) of facilitating or engaging in Federal criminal activity.
Use of Tax Information in Administrative or Judicial Proceedings In general, returns or return information disclosed by the IRS to a Federal agency may be entered into evidence in any administrative or judicial proceeding pertaining to enforcement of a specifically designated Federal criminal statute (not involving tax administration) to which the United States or the agency is a party. However, a return or return information that was disclosed pursuant to a court order may be entered into evidence only if the court finds that it is probative of a matter in issue relevant in establishing the commission of a crime or the guilt of a party.	Use of Tax Information in Administrative or Judicial Proceedings In general, tax information that is disclosed under the provisions of the bill could be entered into evidence in accordance with the Federal Rules of evidence, or other applicable law, in any administrative, judicial, or grand jury proceeding pertaining to enforcement of a specifically designated Federal criminal statute (not involving tax administration) or in any ancillary civil proceeding to which the United States or any Federal agency is a party.	Use of Tax Information in Administrative or Judicial Proceedings Similar to H.R. 1502.
Disclosure of Tax Information in Emergency Circumstances No provision.	Disclosure of Tax Information in Emergency Circumstances Under emergency circumstances that involve an imminent danger of physical injury to any person, serious physical damage to property, or flight from prosecution, the IRS could disclose any information (return information and nonreturn information) to the extent necessary to apprise the appropriate Federal agency of the emergency. The IRS would be required to notify the Justice Department that such a disclosure had been made. The Justice Department then would notify the appropriate U.S. district court judge or magistrate that such a disclosure had been made.	Disclosure of Tax Information in Emergency Circumstances Similar to H.R. 1502.

Present Law	H.R. 1502	S. 1891
Assistance of IRS in Joint Tax and Nontax Investigation No provision.	Assistance of IRS in Joint Tax and Nontax Investigation The bill would provide that the disclosure restrictions could not be interpreted to preclude or prevent the IRS from assisting the Justice Department or any other Federal agency in joint tax and nontax investigations of criminal matters that may involve income tax violations. Moreover, the disclosure restrictions could not be interpreted to preclude or prevent the IRS from investigating or gathering relevant information concerning persons engaged in criminal activities that may involve tax violations.	Assistance of IRS in Joint Tax and Nontax Investigation Similar to H.R. 1502.
Redisclosure of Tax Information to State Authorities No provision.	Redisclosure of Tax Information to State Authorities Under the bill, any official who is authorized to apply for disclosure could apply to a Federal district court judge or magistrate for an *ex parte* order to disclose any return or nonreturn information in his possession, which is relevant to the violation of a State felony statute, to the appropriate State attorney general or district attorney. The disclosure application would set forth: (1) the name and address of the taxpayer, (2) the taxable period or periods to which the information relates, (3) a description of the information sought to be disclosed, and (4) the State felony violation involved. Disclosure would be made to a State attorney general or district attorney if a Federal district court judge or magistrate determined that: (1) there is reasonable cause to believe, based upon information believed to be reliable, that a specific State felony violation has occurred or is occurring and (2) there	Redisclosure of Tax Information to State Authorities Similar to H.R. 1502, except that before disclosure were made to a State attorney general or district attorney, it would also have to be determined that the information would be disclosed exclusively for use in a State criminal investigation or proceeding concerning the State felony violation.

Present Law	H.R. 1502	S. 1891
	Redisclosure of Tax Information to State Authorities (cont'd.) is reasonable cause to believe that the information may be relevant to a matter relating to the commission of the violation.	
Disclosure to Competent Authority Under International Treaty or Convention In general, a return or return information may be disclosed to a competent authority of a foreign government that has a treaty relating to the exchange of tax information with the United States. This information may be disclosed only to the extent provided in, and subject to the terms and conditions of, such treaty.	Disclosure to Competent Authority Under International Treaty or Convention The bill would permit disclosures of tax information to foreign governments, pursuant to mutual assistance treaties, for use in nontax criminal matters. This disclosure would be permitted through a court order upon a finding by a district court judge or magistrate that: (1) there is reasonable cause to believe that the information sought may be relevant to a matter relating to the commission of a specific criminal act that has been committed, or is being committed, against the laws of a foreign country and (2) the information is sought exclusively for use in the foreign country's criminal investigation or proceeding concerning such criminal act.	Disclosure to Competent Authority Under International Treaty or Convention Similar to H.R. 1502.
Foreign Intelligence Access No provision.	Foreign Intelligence Access No provision.	Foreign Intelligence Access The bill would permit the disclosure of investigative return and nonreturn information to the Attorney General upon personal certification by the Attorney General that the information is sought exclusively for use in foreign intelligence collection or a foreign counterintelligence investigation and that there is reasonable cause to believe that the subject of the information is or may be (1) engaged in espionage, sabotage, clandestine intelligence activities, or international terrorism pursuant to the direction of a foreign power; (2) the actual target of an active effort

Present Law	H.R. 1502	S. 1891
		Foreign Intelligence Access (cont'd.) by a foreign intelligence service or international terrorist organization involving positive steps to accomplish recruitment; or (3) furnishing or about to furnish national defense information, sensitive economic or technological information or materials, or foreign policy information to a representative of a foreign power or foreign intelligence service.
Criminal Penalties for Unauthorized Disclosure of Tax Information The maximum criminal penalty for the unauthorized, willful disclosure of tax information is $5,000 and 5 years imprisonment.	Criminal Penalties for Unauthorized Disclosure of Tax Information The bill would provide an affirmative defense to prosecution where the disclosure of tax information was made pursuant to a good faith but erroneous interpretation of the law.	Criminal Penalties for Unauthorized Disclosure of Tax Information Similar to H.R. 1502.
Civil Damages for Unauthorized Disclosures of Tax Information In general, present law provides that any person who willfully or negligently discloses returns or return information in violation of the law may be liable for damages sustained by the taxpayer.	Civil Damages for Unauthorized Disclosures of Tax Information The bill provides that if a Federal employee knowingly or negligently discloses returns or nonreturn information with respect to a taxpayer in violation of the law, then the taxpayer who has been wronged may bring a civil action for damages exclusively against the appropriate Federal agency.	Civil Damages for Unauthorized Disclosures of Tax Information Similar to H.R. 1502.
	Effective Date The provisions would be effective upon enactment.	Effective Date The provisions would be effective upon enactment.

that the disclosure would identify a confidential informant or seriously impair a civil or criminal tax investigation.[23] Tax information other than returns or return information supplied by or on behalf of a taxpayer is available to any Federal agency for use in non-tax criminal investigations upon written request of the head of the agency or, if the request is from the Justice Department, the Attorney General, Deputy Attorney General, or an Assistant Attorney General, and the Treasury Secretary can refuse to supply such data on the same grounds as noted above.[24]

The Treasury Department personnel are also permitted voluntarily to initiate disclosure to the Justice Department of tax data, other than returns and information supplied by or on behalf of the taxpayer, which the Treasury Secretary believes may constitute evidence of a violation of Federal criminal laws.[25]

A Federal agency which has properly received tax information, including returns and tax return information, may disclose it in an administrative hearing or trial only if there is a showing to the presiding hearing officer or judge that the return or data is probative of a matter in issue relevant to the establishment of the commission of a crime.[26]

---

[23] Int. Rev. Code of 1954 § 6103(i)(1).

[24] Int. Rev. Code of 1954 § 6103(i)(2).

[25] Int. Rev. Code of 1954 § 6103(i)(3).

[26] Int. Rev. Code of 1954 § 6103(i)(4).

III. ANALYSIS OF S.732 AND H.R. 1502 (97th Congress)

In recent years a number of observers have concluded that the standards and limits on disclosure are unreasonably high, imposing nearly insuperable barriers to disclosure for law enforcement purposes. They suggest that the law can be amended to facilitate law enforcement without undue infringement on taxpayer privacy. S.732 (97th Cong.) is an attempt to meet this perceived need. Among the major changes proposed in that measure are:

1. In nontax criminal cases access to the underlying books and records of larger corporations and partnerships could be gained by the easier written request precedure.

2. Standards for securing disclosure by court order and by written request would be relaxed.

3. IRS would be required to furnish to Federal law enforcement officials information concerning nontax crimes in information furnished by third parties not acting on behalf of the taxpayer.

4. Provision would be made for disclosure to State law enforcement officials and competent authorities of foreign governments in nontax criminal cases.

5. Use of such information as evidence in trials would be eased and authority given for its use in ancillary civil proceedings.

IV. JUSTIFICATIONS FOR AND QUESTIONS RAISED BY PROPOSED CHANGES

Categories of protected information - As noted above the major substantive effect of proposed definitional changes would be to permit disclosure of the underlying books and records of corporations, associations, and partnerships with more than (2) two shareholders, members, or partners by written request rather than by court order as under present law. As justification for the proposal it is urged that corporations do not enjoy the same "constitutional protections" as individuals, do not have the same expectations of privacy, and that other agencies with similar corporate information, such as the SEC are not subject to disclosure prohibitions preventing them from turning information about criminal activities over to the Justice Department.[5] On the other hand, it may be suggested that there is no real basis for distinguishing between a corporation with three shareholders and one with three or four; that personal information may be contained in the records of large corporations; that corporations do enjoy many constitutional guarantees; and that if the proposals to ease court ordered access contained in S.732 are accepted, there may be less reason to deny them the protection of the court order procedure.[6/]

---

[5] Cong. Record (daily ed.) for Mar. 17, 1981 at S.2303.

Court ordered disclosure - There seems to be little controversy over certain proposed changes in this area including 1) permitting United States Magistrate to issue such orders, 2) eliminating authority of Federal agency heads to apply for such orders and limiting initial access to the Department of Justice, and 3) permitting attorneys in the field, United States Attorneys or the head of an organized crime strike force, to apply for such orders. In support it is noted that 1) Magistrates already possess power to issue search warrants, an analogous order; 2) criminal law enforcement is primarily a Justice Department activity, and other agencies rarely have need for such information; 3) field attorneys have primary responsibility for criminal law enforcement, requiring access to such information, and there is no reason to require approval from Washington to seek a court order, since such approval is generally pro forma and does not significantly add to protection of taxpayer privacy, which is served primarily by the requirement of review of the application by a United States District Judges or Magistrate.[7/]

[6/] Statement of William J. Anderson, Director General Government Division (U.S.G.A.O.) before the Subcommittee on Oversight of the Internal Revenue Service, Senate Committee on Finance, on the Effects of the 1976 Tax Reform Act's Disclosure Provisions on Law Enforcement Activities; November 9, 1981. While corporations do not enjoy 5th Amendment protection against self incrimination (Hale v. Henkel, 201 U.S. 43 (1906)), they do enjoy other constitutional guarantees including 4th Amendment protection against an unreasonable search and seizure (Silverthorne Lumber Co. v. United States, 251 U.S. 385 (1920)) and 1st Amendment freedom of speech protection (First National Bank v. Bellotti, 435 U.S. 765 (1978)).

[7/] Review of Taxpayer Privacy Issues, Hearings, Subcommittee on Oversight of the House Ways and Means Committee, 96th Cong., 2nd Sess., July 30, 1980 at 68-69, 82-83 (statement of Deputy Attorney General Irvin B. Nathan), 84-85 (statement of Senator Nunn). Rule 41 of the Federal Rules of Criminal Procedure authorizes magistrates to issue search warrants.

More controversial are the proposed modifications in the standards for granting a court order, which would eliminate the need for demonstrating that there is reason to believe the information is "probative evidence" of the commission of a criminal act and that it is either not otherwise "reasonably" obtainable or "the most probative evidence" of the matter at issue, replacing those standards with assurance that the information will only be used for a specified criminal investigation or proceeding and there is "reason to believe" it "may be relevant" to a matter at issue. Justice Department officials argue that, if literally applied, existing standards would be unreasonable because the applicant could only prove that the information was "probative" or "most probative evidence" if he had the information sought. The proposed standard is, they maintain, the standard generally imposed by judges under the present law, who know what applicants can realistically be expected to prove. Elimination of the present provision requiring a showing that the information is not otherwise reasonably available appears to have been the subject of greatest concern to critics of this portion of the proposal. They have noted that 1) a similar requirement is statutorily imposed for court ordered electronic surveillance of oral communications,[8] and 2) there is no reason to require disclosure of taxpayer returns and supporting information furnished IRS, where the necessary information is reasonably available from other sources.[9]

Neither existing law nor S.732 provide for court ordered disclosure initiated by IRS, and hence, if the Service has returns or underlying books and records clearly evidencing nontax criminal activity, it must await a court order applied for by another agency. It has been suggested by some that provisions should be made to permit IRS to apply for a court order in such circumstances.[10] It has also been suggested that an applicant successfully meeting the standards for a court order should be given access to third party information without the necessity of complying with the less stringent written application procedure and any modification of existing law should contain such a provision. S.732 does not.[11]

---

[8] Statement of Senator Weicker, Hearings, *supra* n.6 at 93, 97, and 99; Statement of William J. Anderson of the General Accounting Office, *supra* n.6.

[9] Statement of William J. Anderson of the General Accounting Office, *supra* n.6.

[10] *Id.*

Disclosure pursuant to written request - S.732 would modify existing law to permit written request for information from the Inspector General of an agency and any designee of the Attorney General. It has been urged that in this area, as under court ordered disclosure, the right of initial access should be limited to the Justice Department to protect privacy, insure coordination, and avoid duplication in criminal investigations.[12] Apparently, proponents believe giving the right to request such information to the Inspector Generals will assist them in investigating fraud and corruption in government.[13] Elimination of a statement of reasons why the material sought "is or may be material" to the investigation or proceeding and its replacement with a statement of alleged criminal activity under investigation, as proposed by S.732, is said to be necessary to eliminate the same "Catch 22" situation found in the existing court order procedure. The agency, it is said, must give "specific reasons" why the information "is or may be material, and this cannot be done without first seeing the material.[14] The formal written request procedure in the Right to Financial Privacy Act authorizes a request to financial institutions for records "only if - ... there is reason to believe that the records soughts are relevant to

---

11/ *Id.* and see statement of Deputy Attorney General Edward C. Schmults before the Subcommittee on Oversight of the Internal Revenue Service, Senate Committee on Finance, concerning Disclosure of Tax Information for Use in Non-tax Criminal Cases, November 9, 1981.

12/ Statement of William J. Anderson (GAO), *supra* n.6.

13/ *Cong. Record* (daily ed.) for Mar. 17, 1981 at S.2306 (introductory statement by Sen. Nunn).

14/ *Id.* at S.2302; statement of William J. Anderson (GAO), *supra* n.6.

a legitimate law enforcement inquiry." (15 U.S.C. § 3408). That provision appears to impose a higher standard for access to a record in the possession of a bank than S.732 would impose for similar information in the hands of IRS. Objection to the existing standard may, in part, result from the requirement that the agency give "specific reasons" why the information "is or may be material," and if that is the case, consideration might be given to providing that "reasons" be given as to why it is believed that information "may be relevant" to the investigation or proceeding.

Further disclosure to other government personnel and witnesses - As noted above, S.732 would specifically authorize the attorney or officer given initial access to IRS information to redisclose to such other government personnel or witnesses as he may deem necessary to assist in the nontax criminal investigation or proceeding. Present regulations and practice apparently permit such disclosure to both government personnel and witnesses.[15] Proponents argue that the specific grant of authority would not change existing practice, that such disclosure is necessary in investigations and trial preparation, and that a similar provision is included in Rule 6(e) of the Federal Rules of Criminal Procedure, permitting government attorneys to disclose confidential grand jury proceedings where they deem it necessary. Rule 6(e) does not, however, permit pretrial disclosure to witnesses, limiting authority to disclose to government personnel.[16] Opponents of the proposed redisclose provision also suggest that the analogy to Rule 6(e) is inappropriate because the government cannot compel self incriminating testimony in a grand jury proceeding.[17]

---

[15] IRS Reg. § 301.6103(i)-1; U.S. Att'y. Man. (Mar. 17, 1981) 9-4.920 *et seq*. governs investigative disclosures. 9-4.922 provides: "Disclosure may be made where necessary to properly interview, consult, depose, or interrogate or otherwise obtain relevant information from any witness who may be called to give evidence in a proceeding resulting from the investigation."

[16] *United States* v. *Bazzano*, 570 F.2d 1120, 1125-1126 (3rd Cir. 1977).

Disclosure to state and local law enforcement officials - S.732 would alter present law to authorize a government attorney given access to confidential information to apply for a court order for redisclosure to the appropriate State attorney general or district attorney of any such information which is "relevant to the violation of a State felony statute." While officials of the Justice Department in the Carter administration expressed opposition to this provision, the present Deputy Attorney General has expressed support for such a proposal.[18] Proponents maintain that the court order provision would provide adequate protection for privacy interests, while providing a needed mechanism for transfer of evidence for prosecution of state law violations to appropriate authorities. Some critics have argued that disclosure of this type would unjustifiably sacrifice privacy rights and expectations for law enforcement coordination.[19] It has also been suggested that there is a potential for political abuse in such disclosures,[20] and that, even if there is a need for such a provision, it should be modified to provide greater protection of privacy interests by limiting initial access to State attorney generals and insuring accountability.[21] If the latter view is accepted, S.732 might be modified to make it clear that the safeguard and record keeping requirements of 26 U.S.C. 6103(p)(4) apply to such disclosures. Those safeguards do and would, under S.732, continue to apply to disclosure to state tax officials for tax purposes and to federal agencies where disclosure of confidential information is made for nontax criminal purposes. Their application to the proposed disclosure for State law enforcement purposes should reduce the potential for abuse and aid in making recipients accountable.

---

[17] Review of Taxpayer Privacy Issues, supra n.7 at 138-139 (statement of John Shattuck, American Civil Liberties Union, Washington Office).

[18] Id. at 74 (statement of former Deputy Attorney General Nathan); statement of Deputy Attorney General Schmults, supra n.11.

[19] Review of Taxpayer Privacy Issues, supra n.7 at 139 (statement of John Shattuck of ACLU).

[20] Id. at 97, 100 (statement of Sen. Weicker).

[21] Statement of William J. Anderson (GAO), supar n.6.

IRS initiated disclosure - S.732 would require, where present law permits, IRS disclosure of third party information and the underlying books and records of larger corporations, partnerships, etc., containing evidence of nontax criminal activities violative of federal law. It would also provide that evidence of nontax criminal activity, regardless of the source, be furnished to the Department of Justice in cases where a tax prosecution is recommended. Proponents argue that such changes are needed because IRS has been reluctant to exercise the permissive authority under present law, leaving such criminal activities unreported, and that the purpose of the law, promotion of honest reporting, is not served in cases of tax fraud, and there is no reason for not reporting nontax as well as tax violations in such cases.[22] Some have suggested that while a duty to disclose is desirable, the proposal should be modified to make it clear that IRS is obligated only to disclose when such information comes to its attention in the course of its regular activities and is not expected to regularly review its files in search of such information.[23] The General Accounting Office has also suggested that IRS might be authorized to apply for a court

---

22/ Cong. Record (daily ed.) for Mar. 17, 1981 at S.2303 (introductory statement of Senator Nunn).

23/ Statement of William J. Anderson (GAO), supra n.6.

order to disclose in any case where evidence of a nontax federal criminal act contained in taxpayer supplied information comes to its attention.[24/]

Disclosure to competent authorities of foreign governments - Existing law permits such disclosure only for tax purposes under the terms of tax conventions. S.732 would also permit disclosure under terms of mutual assistance treaties for criminal law enforcement purposes. A court order would be required. Proponents suggest this is necessary to insure United States is given reciprocal access to information of criminal activity contained in foreign tax files and that the court order procedure will provide adequate privacy protection.[25/] Critics argue that the privacy rights should not be infringed to assist in foreign law enforcement, since definitions of criminal conduct and concepts of fundamental fairness in such proceedings may vary considerably.[26/]

Disclosure in emergencies - S. 732's provision permitting disclosure by IRS of protected information to the appropriate Federal agency without following ordinary procedures in situations involving imminent danger of injury to person or property or flight to avoid prosecution is justified on the ground that time does not permit compliance with such procedures.[27/] When such a disclosure occurs IRS must inform the Justice Department, as soon as possible, and Justice is to notify the appropriate United States District Court. GAO has suggested that national security emergencies should also be included in this proposed provision and that disclosure to the appropriate State authorities also be

---

[24/] Id.

[25/] Review of Taxpayer Privacy Issues, supra n.7 at 73 (statement of former Deputy Attorney General Nathan).

[26/] Id. at 139 (statement of John Shattuck of ACLU).

[27/] Cong. Record (daily ed.) for Mar. 17, 1981 at S.2310 (introductory statement of Sen. Nunn).

permitted, since such threats may frequently involve potential State law violations, e.g. murder.[28] A similar proposal before the 96th Congress which included a national security provision was criticized on the grounds that the term was too vague to provide adequate guidance and subject to potential abuse. It was also suggested that if such disclosure was permitted, some provision for judicial scrutiny of the disclosure similar to that in the wiretap statute, providing that when an emergency tap is instituted court approval must be sought within 48 hours, should be included.[29]

Use as evidence in judicial and administrative proceedings - The feature of the proposed changes in this area likely to generate the most controversy is that permitting use of protected information in civil proceedings which are "ancillary" to nontax criminal proceedings. Generally, an ancillary proceeding is one in aid of, supplementary to, or subordinate to another primary action.[30] If the term is used as generally applied, privacy interests would not be adversely affected since presumably public disclosure in a nontax criminal proceeding will or would have occurred. However, the introductory statement indicates that it is intended to permit use in civil proceedings where they are used in lieu of a possible criminal proceeding as well.[31] GAO noted that, since disclosure can occur only for a nontax criminal investigation or proceeding, it will not be available where the decision has been made to pursue only civil investigations and proceedings involving activities with criminal overtones, such as a forfeiture proceeding for controlled substances under 21 U.S.C. § 881, and that consideration might be given to providing for a transfer of information in such cases.[32] Objections to proposals to allow such use in civil proceedings in hearings in 1980 included a suggestion that, at a minimum, respect for the privacy of the taxpayer required the attorney seeking to make use of such information to establish a link between the civil proceeding and the criminal investigation or proceeding for which the evidence was originally disclosed.[33]

---

[28] Statement of William J. Anderson (GAO), supra n.6.

[29] 18 U.S.C. § 2518(7); Review of Taxpayer Privacy Issues, supra n.7 at 93 (statement of Sen. Weicker).

[30] See the definition of ancillary proceeding in Black's Law Dictionary (4th ed.); Schram v. Roney, 30 F. Supp. 458 (E.D. Mich. 1939).

[31] Cong. Record (daily ed.) for March 17, 1981 at S.2306.

Assistance in joint tax/nontax criminal investigations - As noted above, S.732 would provide for the transfer of evidence to the Justice Department of nontax criminal conduct in any case where a criminal tax prosecution was referred. In addition it provides that nothing in the statute is intended to prevent IRS from assisting other Federal agencies in joint tax/nontax investigations. It has been suggested that this provision is unclear as to whether, in such a situation, disclosure procedures are still applicable or are overriden.[34]

Civil and criminal sanctions for violating the statute - Changes in these provisions making the Federal agency instead of the individual employee, civilly liable for damages and permitting the defendant in a criminal case to defend on the basis of a good faith but erroneous interpretation of the statute are the least controversial of the proposed changes in existing law contained in S.732. The proposed affirmative defense in criminal proceedings is already provided in the civil damage provision.[35]

32/ Statement of William J. Anderson (GAO), *supra* n.6.

33/ *Review of Taxpayer Privacy Issues*, *supra* n.7 at 139 (statement of John Shattuck of ACLU).

34/ Statement of William J. Anderson (GAO), *supra* n.6.

35/ 26 U.S.C. § 7217.

○